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SKYPE – LESSONS LEARNED FROM A HISTORY OF SUCCESS AND FAILURE IN
MERGERS AND ACQUISITIONS

Regulatory Approval and Cisco Challenge - SIMON HUSCAVA - 59452

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Abstract (100 words maximum)

The eventful acquisition history of Skype first gained attention in 2005 with eBay's \$2.6 billion takeover of the then-unprofitable VoIP technology company. eBay's failed attempts to integrate the software into its bidding platform and an associated \$1.4 billion write-down illuminated the importance of credibility of synergies in the context of Mergers & Acquisitions. A subsequent majority stake sale to private equity investors at a \$2.75 billion valuation and two attempted public floats later, Microsoft announced the staggering \$8.5 billion acquisition that led to speculations about merger motives and raised concerns around competitive dynamics and merger control.

Keywords (minimum of four):

Mergers & Acquisitions (M&A), Corporate Finance, Synergies, Case Study, Company Analysis

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Part A: Case Study

“This is a big day for Skype and this is a big day for Microsoft. We are adding a new division and a new promise to our customers, the promise of universal next-generation communications. Microsoft and Skype together will bring together hundreds of millions, or as Tony said, billions of consumers and empower them to communicate in new and interesting ways.”

Steve Ballmer, Microsoft CEO (Microsoft Corp. 2011a)

“We really appreciate the fact that, Steve, you have put your faith in us. We think there is a tremendous amount of opportunities as we look forward. We think this allows us to extend now from hundreds of millions to literally billions. We believe that this is a platform and a set of services that can reach everyone on the planet.”

Tony Bates, Skype CEO (Microsoft Corp. 2011a)

On May 11th, 2011, the top executives of Microsoft and Skype hosted a call to announce Microsoft’s \$8.5 billion acquisition of the rapidly expanding communications service company. The move came after its owners, a private equity consortium led by Silver Lake, published a preliminary IPO prospectus with plans to float Skype just one year earlier, as well as reported talks with both Facebook and Google about an acquisition in the week leading up to the announcement (Halliday 2011). While this made it apparent that Skype was a contended asset in a reviving tech market in the aftermath of the great financial crisis, big question marks kept surrounding the deal. Most importantly, was Skype worth \$8.5 billion, a staggering 10 times sales and 32 times EBITDA, considering its turbulent acquisition history and most recent valuation of \$2.75 billion just three years earlier? Would this acquisition – by far Microsoft’s largest at the time – aid the maturing company that was struggling to catch up with its fast-growing, dynamic peers such as Apple and Google?

Microsoft Corporation

Founded in 1975 by Bill Gates and Paul Allen, Microsoft quickly rose to prominence as a global technology leader, revolutionizing personal computing with its Windows operating system and Office productivity suite. Throughout the 1980s and 1990s, the company dominated the software market, establishing itself as a household name and one of the most valuable companies in the world.

In 2011, Microsoft was a dominant yet somewhat stagnant player in the technology industry. Despite being highly profitable, with strong revenue streams from its Windows operating system and Office suite, the company was increasingly viewed as a mature giant struggling to innovate in a rapidly evolving tech landscape. Microsoft's core business remained focused on enterprise solutions and PC software, but it faced significant challenges in emerging markets like mobile computing and cloud services, where competitors such as Apple, Google, and Amazon were gaining ground (Zachary, Hall, and Montevirgen 2024).

Investor sentiment reflected these concerns, with Microsoft's stock having remained relatively flat for much of the previous decade. Although the company had vast cash reserves, which allowed for strategic acquisitions like Skype, there was growing skepticism about its ability to remain competitive and innovative, particularly in the consumer tech space. In contrast, companies like Apple were thriving on the success of the iPhone and iPad, Google was rapidly expanding with Android and cloud services, and Amazon was making significant strides with AWS. In its 2010 Annual Report, Microsoft similarly tried to convince investors of its innovation capabilities in core focus areas such as communication and collaboration at work, foreshadowing the Skype deal:

"We continue to develop innovative software applications and solutions that we believe will enhance information worker productivity, improve communication and collaboration in work

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groups, aid business intelligence, and streamline processes for small and mid-sized businesses.“ (Microsoft Corp 2010a)

Skype Global S.á.r.l.

Founded in 2003 by Niklas Zennström and Janus Friis, Skype transformed the telecommunications landscape with its pioneering use of voice-over-internet protocol (VoIP) technology, allowing users to make voice and video calls over the internet. This innovation significantly altered global communication by enabling free or low-cost calls worldwide. Skype quickly grew into a major player in digital communication, attracting millions of users in a short period and establishing itself as a key platform for both personal and business use.

By 2011, Skype had more than 660 million registered users and had become a leader in online communication. However, it faced increasing competition from newer platforms such as Google Voice and Apple’s FaceTime. While Skype had successfully moved into mobile communication and video calling, concerns persisted about its business model, particularly its reliance on a small number of paying users while most accessed its services for free. The company’s peer-to-peer infrastructure, though innovative, also presented challenges in monetizing its vast user base. (Skype S.á.r.l. 2010)

Skype's history of mergers and acquisitions reflected its strategic importance in the tech industry. In 2005, eBay purchased Skype for \$2.6 billion, with the intention of integrating its communication features into eBay’s e-commerce operations. This vision, however, did not deliver the expected benefits, leading eBay to take a \$1.4 billion write-down two years later. In 2009, eBay sold a 65% stake in Skype to an investment group led by Silver Lake Partners for \$1.9 billion, retaining a 35% minority stake. The deal valued Skype at \$2.75 billion, allowing it to operate with more independence and focus on growth. Skype continued to expand under this new ownership, but with competition intensifying, it became the subject of acquisition

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interest from major companies like Google and Facebook, ultimately paving the way for its acquisition by Microsoft in 2011. When the news broke on 30th April 2011 that Microsoft would pay a staggering \$8.5 billion for the communication company, those previous valuations numbers were still in people's minds. Wall Street's generally negative perception of the deal was quickly reflected in the stock price in the days after the announcement, losing 4.3% in the first week (Appendix 3). How the tech giant came up with a valuation that equaled 10 times sales and 32 times EBITDA, representing almost \$1,000 for each of the 8.8 million monthly paying users, was a much-discussed subject. (J. Shan 2013)

Industry Outlook

Skype's noteworthy rise in popularity took place against a backdrop of rapid technological advancements in broadband and Voice over Internet Protocol (VoIP) technology as well as intensifying competition and consolidation in the software & internet services industry.

Significant increases in in-home broadband internet adoption led to an average penetration rate of 24% in OECD countries by the end of 2010 (OECD 2003-2012) (Appendix 1). Elsewhere in tech, the smartphone was taking the world by storm while mobile broadband adoption rates nearly eclipsed 50% in OECD countries by mid-2011 laying the groundwork for Skype's launch on iOS and Android devices in 2010 and 2011 respectively (OECD 2003-2012).

In addition to increased broadband penetration rates Skype deployed an innovative Peer to Peer (P2P) infrastructure distributing the communication load between user's computers which increases call reliability and quality while cutting down on infrastructure costs such as servers (Baset and Schulzrinne 2004), (Wang 2005). Furthermore, video and voice compression algorithms allowed for high quality calls even with lower bandwidths (Anderson 2016).

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As VoIP technology matured alongside broadband adoption, significant challengers to Skype's competitive position emerged in the form of other VoIP providers, big-tech and social media companies as well as traditional telecommunications firms.

While Skype, launched in 2003, was an early adopter of internet telephony software, it was never alone in the space which was pioneered by VocalTec, offering internet telephony, and Net2Phone, which bridged the gap from PCs to landlines, in 1995 and 1996 respectively. Another significant VoIP competitor Vonage, which also offers hardware solutions, was launched in 2001 and quickly became a household name in the space. What allowed Skype to stand out among its peers was its scalability (P2P) and freemium business model which offered user to user calls for free and user to landline calls at affordable rates. Further distinguishing factors helping Skype maintain its competitive position were the program's ease of use and user-friendly interface as well as innovations such as the adoption of group video calls.

Traditional telecommunication giants with a large customer bases and plentiful funding also created VoIP offerings such as AT&T's U-verse Voice and Comcast's Xfinity Voice which amassed 2.1 million and 8.6 million users respectively by 2011 and 2010 (AT&T 2011), (Comcast 2011). A new wave of challengers approached from the Silicon Valley shortly before Skype's acquisition by Microsoft. Google Voice (2009) and Google Hangout (2011) as well as Apple's Facetime (2010) and Facebook's Messenger application all offered voice and video call features. Shortly after this launch wave of new VoIP programs Skype itself was acquired by Microsoft and integrated into its ecosystem which already included the Windows Live Messenger (formerly MSN) communication platform.

In 2012 Skype reached 167 billion minutes of international telephone traffic, excluding PC to PC calls. At the time this represented 33% of international phone traffic disrupting the traditional telecommunication industry (Exhibit 1).

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The merger was part of an uptick in M&A activity in terms of transaction volume following the 2008 financial crisis. After the total transaction value in the Software & Internet Services sector bottomed out at \$42 billion in 2009 it recovered to \$79 billion in 2011 (Institute for Mergers, Acquisitions & Alliances 1997-2013) (Appendix 2).

Deal Talks Begin

Based on the industry outlook and the services and products Microsoft and Skype offered, the deal talks begin. Steve Ballmer stated that the takeover of Skype will bring together the best world of both companies, since Microsoft offers a large variety of products like its office and home services, which are going to be enhanced through the communication technology of Skype. Therefore, Microsoft's dream about building experiences that aren't limited by distance or device could be achieved by bringing people together, whether it is on a single screen, a smartphone, a PC, a slate, or the simple TV through the achieved synergies by the acquisition of the established and well-known brand Skype. Moreover, Mr. Ballmer pointed out that Skype has more than 660 million registered users and a growth of 600,000 customers per year, which indicated the importance and the upside potential of modern communication technology. Furthermore, Microsoft was aware that its main competitors would also take steps towards the communication market or have already done so. Therefore, the company did not want to be in the position of being unable to compete (Microsoft Corp. 2011a). Tony Bates also made clear that Skype, which is headquartered in Luxembourg, is growing at rapid speed, fueled by several key opportunities. First, the core communications technology was highly synergetic with Microsoft's current products and services. Second, the large and engaged user base may be utilized as a key part of the company's new monetization strategy by adding a premium subscription packages layer, new advertising avenues and more. Furthermore, Skype's profitable sound business will add to Microsoft's bottom line and cash flow (Microsoft Corp.

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2011a). The two companies had high hopes that an acquisition would bring advantages to both sides and that their strategies could be implemented more quickly by the knowledge the other offers. On top of that, the traded all-cash purchase price of \$8.5 billion seems attractive for Skype's current investors.

Now the question arises for Microsoft's management: are the parties deceived by only looking at positive aspects, or is the high purchase price justified for a company with a difficult acquisition and valuation history?

Timeline of Events (Intellectual Asset Management Magazine 2011)

<i>August 2003</i>	Skype is founded by Niklas Zennström and Janus Friis
<i>April 2005</i>	Skype user base grows rapidly, hitting the 100 million downloads mark
<i>September 2005</i>	eBay announces the acquisition of Skype for \$2.6 billion
<i>October 2007</i>	eBay takes a \$1.4 billion write-down on Skype, stating that “the company’s handling of the Skype buy-out had been a mistake”
<i>April 2009</i>	eBay announces the planned IPO of Skype, detailing that although it is a great standalone business ... Skype has limited synergies with eBay
<i>September 2009</i>	Skype IPO is called off after a series of legal disputes with co-founders relating to IP. Zennström and Friis allege that Skype is in breach of a licensing agreement with Joltid, a company owned by the co-founders that owns the IP for Skype’s peer-to-peer technology.
<i>November 2009</i>	eBay gives up a 14% stake in Skype to Joltid as part of a settlement and sells a majority stake to a private equity consortium for \$2.75 billion

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August 2010 Skype announces plans to float in an IPO, publishing a preliminary prospectus that contains valuable information for potential buyers about the private company

May 2011 Microsoft announces the acquisition of Skype

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Regulatory Approval and Cisco Challenge

After Microsoft and Skype announced their merger agreement to the public in May 2011, in early September of 2011 the parties formally notified the European Commission of their plans to obtain the regulatory greenlight for the consummation of the merger.

a. Affected Consumer Markets

In their investigation the European Commission (EC) identified that the merger would concern the Internet Consumer and Enterprise Communications market (“Consumer and Enterprise Communications”). For the purpose of their assessment, the EC segmented the market into Consumer Communications Services and Enterprise Communications Software Services (European Commission 2011).

1. Consumer Communications Services

The European Commission (2011) described the consumer communications services market as a nascent and growing sector which was shifting from PCs to smartphones and tablets. Instant messaging (IM) was declining on PCs but experienced significant growth on other devices and embedded into other services (e.g. Facebook). The voice calls segment saw considerable growth due to technological advancements and saw an increasing number of market participants including Facebook, Google, Viber. Video calls were projected to increase from 3.2 billion in 2011 to 29.6 billion in 2015. By 2015, 40% of this growth was projected to come from non-PC

devices. Most consumer communications services were free of charge, indicating a high consumer price sensitivity. Skype estimated that [>75] % of its users would cease to use the service if they started to generally charge for it. The market was also characterized by short innovation cycles as consumers in the space placed great importance on product innovations (European Commission 2011).

2. Enterprise Communications Services

The enterprise communications services market was also characterized by rapid growth. It was forecasted that [80-90] % of companies with over 50 employees intended to use enterprise communications platforms in the subsequent years. Such software typically included features such as audio- and video conferencing for a large number of participants, instant messaging, file sharing, co-editing of documents and more. Also, there was a growing trend towards mobile devices in this segment (European Commission 2011).

“Other technologies are emerging. If these succeed, it may render Skype a relic” – lawyer representing the EC (Reuters 2013).

b. Market Shares

According to self-reported market share estimations, the addition of Skype with [0-5] % market share to Microsoft would have left market shares in Instant Messaging (IM) unchanged (Exhibit 22). In the voice call segment, the merging parties submitted an estimation that Skype held a [40-50] % market share of international VoIP carrier and PC to PC traffic. The combining parties believed that adding this to the approximate share of [0-5] % held by Windows Live Messenger (“WLM”) would result in a combined market share of [40-50] %. Lastly, post-merger market shares in the video call segment (Exhibit 23) would have amounted to around [80-90] % in the EEA with a similar value estimated worldwide (European Commission 2011).

In the Enterprise Communications market, the parties submitted that the share of Skype users using the platform exclusively for business was around [5-10]%, comprised mostly of SMEs. In the SME Enterprise Communications segment, Microsoft had a market share of [0-5]%. When considering a market for IM and voice- and video calls for businesses, Microsoft's Lync had an estimated [10-20]% market share behind Cisco [30-40]% and ahead of Citrix and IBM. Skype's market share was estimated at [0-5]% (European Commission 2011).

c. Cisco Challenge

After a thorough investigation and hearing of complaints by stakeholders invited to the process, the EC approved the merger in October of 2011 without conditions. Antitrust regulators previously did not shy away from blocking similar mergers such as those of Microsoft and Intuit in 1994 and AT&T and T-Mobile in 2011. Azertac (2011) wrote about the approval: "With tensions over this case and others, getting approval from the EC without even a second look is impressive".

After the EC gave its greenlight for the merger, in February 2012, Cisco Systems and the Italian VoIP provider Messagenet challenged the decision in the General Court of the European Union. *"The European Commission conducted a thorough investigation of the acquisition, in which Cisco actively participated, and approved the deal in a 36-page decision without any conditions"* – Unnamed Microsoft Spokesperson (Berndtson 2012)

Their main points of contention with the ruling on the consumer communications market included:

- failure to properly address network effects between WLM and Skype in video calls on Windows PCs which might give rise to entry barriers
- the very high combined market shares in some markets should warrant additional scrutiny

- failure to bring forth evidence of the capacity of consumers to switch services
- EC improperly assessed the competitive pressure the new entity would face

Regarding enterprise communications services the applicants objected that:

- Not all complaints of interested parties (including Cisco) during the initial merger decision process regarding a potential exclusionary strategy of the merged entity were addressed
- The EC failed to evaluate the ability and incentive of the new entity to use its position in consumer communications (especially in video calls) as leverage to impact competition on the enterprise communications market

"We respect the European Commission and value Microsoft as a customer, supplier, partner and competitor. Cisco does not oppose the merger, but believes the European Commission should have placed conditions that would ensure greater standards-based interoperability, to avoid any one company from being able to seek to control the future of video communications."

– Marthin de Beer, Senior VP of Cisco's Emerging Business Group (Berndtson 2012)

"The merger created an effective monopoly and condemned competitors to a niche." – Cisco's lawyer to the judge (Reuters 2013).

After further fact-finding and hearings, the General Court of the European Union issued a ruling on the application for annulment of the merger on the 11th of December 2013 (General Court of the European Union 2013).

d. Killer Acquisition

The term killer acquisition describes the concept of incumbent firms acquiring innovative companies in order to stifle innovation and prevent future competition (Cunningham, Ederer, and Ma 2021). While the concept has existed for a longer time, it gained renewed prominence in the 2010s alongside increasing consolidation in tech and life sciences. The 2021 paper by

Cunningham, Ederer, and Ma renewed such concerns by adding to the theoretical literature concrete empirical evidence of killer acquisitions in the pharmaceutical sector. As a reaction to the renewed interest in the issue, the EC introduced the article 22 of the EUMR (EU Merger Regulation) referral mechanism, allowing for the investigation of below threshold mergers that might impact competition (Norton Rose Fulbright 2024). This aimed to close a blind-spot of merger reviews of takeovers of low-revenue, innovative companies that might get swept up in a killer acquisition which tend to be smaller companies and start-ups. In the US, in 2021, President Joe Biden issued an executive order urging antitrust agencies to emphasize innovation and fair competition in their merger reviews. In 2023, merger guidelines were revised to explicitly include innovation harm as a critical focal point (U.S. Department of Justice and the Federal Trade Commission 2023).

This new wave of attention and scrutiny was also met with criticism by papers such as Madl (2020) and Barnett (2024), who argue that the findings by Cunningham, Ederer, and Ma (2021) were, inter alia, due to the structure of the pharmaceuticals market and the fact that there is no evidence that killer acquisitions are a widespread phenomenon across industries. Both papers view blanket scrutiny of such overlapping transactions critically arguing that it would significantly heighten transaction costs while bringing negligible welfare gains for consumers. Barnett (2024) also highlights how increased scrutiny might put into jeopardy the critical, widely documented, monetization mechanism of incumbent firm's acquisitions of contenders where larger acquirers provide funding and scale efficiencies to low-revenue, innovative targets.

“First, and I’ve got to underscore this, we’re committed to the Skype user base. Today and into the future we want to continue to build and engage that base, as Skype is doing today. [...] Our vision is that products and services that Skype users know and love today will simply grow and

be enhanced. Part of that commitment is to continue investing and supporting Skype on non-Microsoft client platforms.”

“We will continue to support non-Microsoft platforms, because it’s fundamental to the value proposition of communications” -Steve Ballmer, Microsoft CEO (Microsoft Corp. 2011a)

e. Decision Point

It is one month before the announcement of the ruling of the General Court of the European Union on the Cisco challenge. An external legal counsel to Microsoft is hired to give a third-party opinion, re-evaluating why the deal was initially approved in spite of a high-combined market shares in some sub-segments and possible conglomerate effects. Furthermore, Microsoft requires an assessment on whether the challenge of Cisco poses a credible threat to the already approved merger.

Exhibits

Exhibit 1: International Telephone & Skype Traffic between 2005-2012 in Billion Minutes (Crabtree 2013)

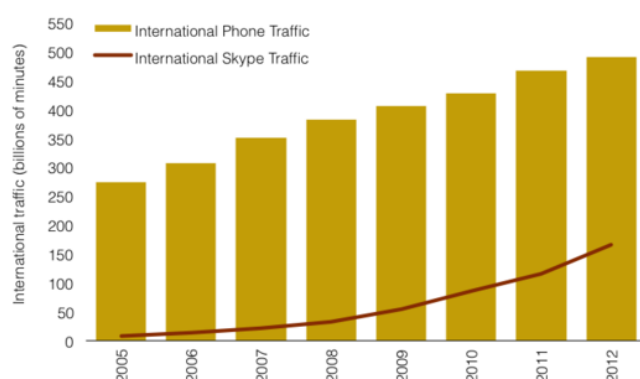


Exhibit 2: Development of Number of Users concurrently online on Skype during peak Activity between 2004-2013 in Millions (Richter 2013)

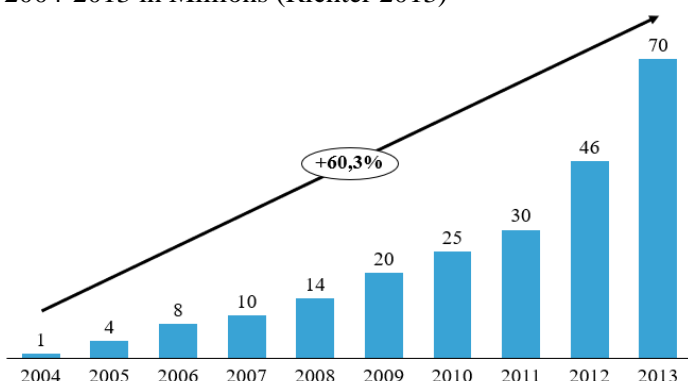


Exhibit 3: Skype's selected Balance Sheet Data (in \$000s)

	2006	2007	2008	2009	2010
ASSETS					
Cash and cash equivalents	\$92 837	\$115 884	\$260 187	\$114 077	\$142 465
Total current assets	\$121 953	\$154 234	\$319 804	\$202 445	\$243 387
Property and equipment	\$7 123	\$9 075	\$6 040	\$13 238	\$36 523
Goodwill	\$2 575 931	\$1 919 341	\$1 836 562	\$2 372 779	\$2 372 779
Intangible assets, net	\$235 711	\$188 204	\$112 934	\$788 118	\$637 688
Total assets	\$2 944 758	\$2 275 410	\$2 282 535	\$3 409 704	\$3 317 855
LIABILITIES AND EQUITY					
Accrued expenses and other current liabilities	\$39 658	\$46 359	\$65 159	\$90 952	\$121 100
Deferred revenue and user advances	\$56 219	\$89 419	\$108 012	\$142 600	\$176 681
Total current liabilities	\$111 740	\$170 463	\$219 893	\$302 246	\$353 726
Long-term debt	\$0	\$0	\$0	\$772 220	\$686 348
Total liabilities	\$150 730	\$186 007	\$222 493	\$1 172 131	\$1 071 165
Total stockholders' equity	\$2 794 028	\$2 089 403	\$2 060 042	\$2 237 573	\$2 246 690
Total Liabilities and Equity	\$2 944 758	\$2 275 410	\$2 282 535	\$3 409 704	\$3 317 855

Sources: Skype's IPO registration statement filing

Exhibit 4: Skype's user matrix (Skype S.à.r.l. 2010)

Users matrix (in millions, besides the \$)	2008	2009	2010
Registered users	325	474	663
Average monthly connected users	75	105	145
Average monthly paying users	5,8	7,3	8,8
Average communications services revenue per paying user	\$102	\$98	\$97
Communications services billing minutes	6900	10700	12800

Sources: Skype's IPO registration statement filing

Exhibit 5: Skype's selected Statement of Operations (in \$000s) (Skype S.à.r.l. 2010)

	2006	2007	2008	2009	2010
Net revenues	\$193 696	\$381 551	\$551 364	\$718 903	\$859 815
Cost of Revenues	\$140 107	\$229 496	\$293 201	\$343 981	\$415 702
Gross Profit	\$53 589	\$152 055	\$258 163	\$374 922	\$444 113
Operating Expenses					
Sales and marketing	\$59 787	\$64 304	\$83 222	\$120 989	\$131 939
Product development	\$38 900	\$22 857	\$33 599	\$45 027	\$72 263
General and administrative	\$37 865	\$42 423	\$48 648	\$160 962	\$104 954
Amortization of acquired intangible assets	\$60 156	\$65 514	\$69 832	\$68 737	\$114 308
Litigation settlement	\$0	\$0	\$0	\$343 826	\$0
Impairment of goodwill	\$0	\$1 390 938	\$0	\$0	\$0
Total operating expenses	\$196 708	\$1 586 036	\$235 301	\$739 541	\$423 464
Loss/Income from Operations	-\$143 119	-\$1 433 981	\$22 862	-\$364 619	\$20 649
Realized loss on amended credit agreement	\$0	\$0	\$0	\$0	-\$13 513
Interest income and other (expense), net	\$2 029	\$5 303	\$10 297	\$2 943	\$4 817
Interest expense	\$0	\$0	\$0	-\$10 387	-\$68 645
Loss/Income before taxes	-\$141 090	-\$1 428 678	\$33 159	-\$372 063	-\$56 692
Income tax (benefit)/expense	-\$22 044	-\$23 342	-\$8 447	-\$3 259	-\$49 787
Net Income	-\$119 046	-\$1 405 336	\$41 606	-\$368 804	-\$6 905
Weighted number of shares, basic and diluted (Class A through J):				9 414 600	9 433 743
Fully Diluted Earnings Per Share before effect of charges					

Sources: Skype's IPO registration statement filing

Exhibit 6: Skype's adjusted EBITDA calculation (in \$000s) (Skype S.à.r.l. 2010)

	2008	2009	2010
Net (loss)/income	\$41 606	-\$368 804	-\$6 905
Income tax (benefit)/expenses	-\$8 447	-\$3 259	-\$49 787
Interest expenses	\$0	\$10 387	\$68 645
Interest (income) and other expense, net	-\$10 297	-\$2 943	-\$4 817
Depreciation and amortization	\$75 534	\$79 049	\$161 297
Stock-based compensation	\$12 826	\$14 746	\$15 950
Realized loss on credit agreement	\$0	\$0	\$13 513
Management Services Agreements with shareholders	\$0	\$1 685	\$14 835
Acquisition transaction fees	\$0	\$98 715	\$1 229
Skype Acquisition transaction bonuses	\$0	\$3 647	\$0
Transition Services Agreement	\$0	\$1 118	\$2 463
Excluded bonus and severance	\$0	\$1 755	\$15 315
Joltid litigation settlement	\$0	\$343 826	\$0
Other litigation settlements	-\$410	\$2 928	-\$784
Separation costs		\$2 054	\$11 312
Foreign exchange gains and losses prior to invoice receipt and related to hedging instruments	-\$334	-\$8	\$12 165
Dispute with payment service provider	\$0	\$0	\$9 247
Non-capitalizable expenses attributable to this offering of securities	\$0	\$0	\$669
Adjusted EBITDA	\$110 478	\$184 896	\$264 347

Sources: Skype's IPO registration statement filing

Exhibit 7: Microsoft's consolidated Balance Sheet (in \$ millions)

	2006	2007	2008	2009	2010
ASSETS					
Cash and cash equivalents	\$6 714	\$6 111	\$10 339	\$6 076	\$5 505
Short-term investments	\$27 447	\$17 300	\$13 323	\$25 371	\$31 283
Accounts receivable	\$9 316	\$11 338	\$13 589	\$11 192	\$13 014
Inventories	\$1 478	\$1 127	\$985	\$717	\$740
Deferred income taxes	\$1 940	\$1 899	\$2 017	\$2 213	\$2 184
Other current assets	\$2 115	\$2 393	\$2 989	\$3 711	\$2 950
Total current assets	\$49 010	\$40 168	\$43 242	\$49 280	\$55 676
Property and equipment	\$3 044	\$4 350	\$6 242	\$7 535	\$7 630
Equity and other investments	\$9 232	\$10 117	\$6 588	\$4 933	\$7 754
Goodwill	\$3 866	\$4 760	\$12 108	\$12 503	\$12 394
Intangible assets, net	\$539	\$878	\$1 973	\$1 759	\$1 158
Deferred income taxes	\$2 611	\$1 389	\$949	\$279	\$0
Other assets	\$1 295	\$1 509	\$1 691	\$1 599	\$1 501
Total assets	\$69 597	\$63 171	\$72 793	\$77 888	\$86 113
LIABILITIES AND EQUITY					
Accounts payable	\$2 909	\$3 247	\$4 034	\$3 324	\$4 025
Short-term debt	\$0	\$0	\$0	\$2 000	\$1 000
Accrued compensation	\$1 938	\$2 325	\$2 934	\$3 156	\$3 283
Income taxes	\$1 557	\$1 040	\$3 248	\$725	\$1 074
Short-term unearned revenue	\$9 138	\$10 779	\$13 397	\$13 003	\$13 652
Securities lending payable	\$3 117	\$2 741	\$2 614	\$1 684	\$182
Other	\$3 783	\$3 622	\$3 659	\$3 142	\$2 931
Total current liabilities	\$22 442	\$23 754	\$29 886	\$27 034	\$26 147
Long-term debt	\$0	\$0	\$0	\$3 746	\$4 939
Long-term unearned revenue	\$1 764	\$1 867	\$1 900	\$1 281	\$1 178
Deferred income taxes	\$0	\$0	\$0	\$0	\$229
Other long-term liabilities	\$5 287	\$6 453	\$4 721	\$6 269	\$7 445
Total liabilities	\$29 493	\$32 074	\$36 507	\$38 330	\$39 938
Total stockholders' equity	\$40 104	\$31 097	\$36 286	\$39 558	\$46 175
Total Liabilities and Equity	\$69 597	\$63 171	\$72 793	\$77 888	\$86 113

Sources: Microsoft's 2006, 2008 and 2010 Annual Reports

Exhibit 8: Microsoft's Income Statement (in \$ millions)

	2006	2007	2008	2009	2010
Revenue	\$44 282	\$51 122	\$60 420	\$58 437	\$62 484
Operating Expenses					
Cost of revenue	\$7 650	\$10 693	\$11 598	\$12 155	\$12 395
Research and development	\$6 584	\$7 121	\$8 164	\$9 010	\$8 714
Sales and marketing	\$9 818	\$11 455	\$13 260	\$12 879	\$13 214
General and administrative	\$3 758	\$3 329	\$5 127	\$3 700	\$4 004
Employee severance	\$0	\$0	\$0	\$330	\$59
Total operating expenses	\$27 810	\$32 598	\$38 149	\$38 074	\$38 386
Loss/Income from Operations	\$16 472	\$18 524	\$22 271	\$20 363	\$24 098
Other income (expense)	\$1 790	\$1 577	\$1 543	-\$542	\$915
Loss/Income before taxes	\$18 262	\$20 101	\$23 814	\$19 821	\$25 013
Provision for income taxes	\$5 663	\$6 036	\$6 133	\$5 252	\$6 253
Net Income	\$12 599	\$14 065	\$17 681	\$14 569	\$18 760
Weighted number of shares outstanding:					
Basic	10438	9742	9328	8 945	8 813
Diluted	10531	9886	9470	8 996	8 927
Earnings per share:					
Basic	\$1.21	\$1.44	\$1.90	\$1.63	\$2.13
Diluted	\$1.20	\$1.42	\$1.87	\$1.62	\$2.10
Cash dividends declared per common share	\$0.35	\$0.40	\$0.44	\$0.52	\$0.52

Sources: Microsoft's annual reports 2006, 2008 and 2010

Exhibit 9: Selected financial data

	Week Ending April 29, 2011
Yields on U.S. Treasury Bills, Notes, and Bonds	
3-month	0,04%
6-month	0,11%
1-year	0,22%
2-year	0,61%
5-year	1,97%
10-year	3,32%
30-year	4,40%
Spreads on Long-term Corporate Bonds	
Aaa	0,59%
Aa	1,01%
A	1,31%
BBB	1,85%
Interest Rates	
Federal Funds	0,09%
3-month Commercial Paper	0,13%
3-month Certificate of Deposit	0,23%
Prime Rate	3,25%
Equity Betas	
Microsoft	0,93
8x8	0,54
BroadSoft, Inc.	0,93
Akamai	1,22
Vonage Holdings Corp.	0,87
Verisign	1,11
ShoreTel, Inc.	1,68
Market Risk Premium	
Market Risk Premium	14,73%
Information out of the IPO Filing	
WACC of Skype	17,00%
Target D/V Ratio of Skype	
Target D/V Ratio	29,33%

Sources: FRED, Federal Reserve Economic Data, Skype's IPO Filing

Exhibit 10: Revenue Synergies (in \$000s)

	Dec 2012E	Dec 2020E
Display marketing services and other revenue	376.500	3.900.000

Exhibit 11: Skype Comparable Companies, 2010 (S&P Capital IQ)

Comparable Companies	Company Description
8x8 Inc.	A VoIP and cloud communications provider with a subscription-based model, directly comparable to Skype's core business.
BroadSoft Inc.	A provider of software solutions enabling telecom service providers to offer VoIP and unified communication services.
Akamai Technologies Inc.	A global leader in content delivery networks (CDN) and cloud services
Vonage Holdings Corp.	A consumer and business-focused VoIP provider, with a subscription-based revenue model similar to Skype.
VeriSign Inc.	A provider of domain name registry services and internet security solutions
ShoreTel Inc.	A company specializing in business-focused unified communication solutions

Exhibit 12: Skype Comparable Companies Financials, 2010 (in \$000s) (S&P Capital IQ)

Company	8x8, Inc.	BroadSoft, Inc.	Akamai Technologies, Inc.	Vonage Holdings Corp.	VeriSign, Inc.	ShoreTel, Inc.
Shareprice (in \$)	3,11	45,48	92,90	5,16	180,77	10,45
Shares outstanding	62.436.804	26.166.000	150.226.986	223.490.000	96.100.000	46.146.000
Market Cap	194.178	1.190.030	13.956.090	1.153.208	17.372.000	482.226
Interest bearing Debt	0	1.970	0	212.452	80.388	0
Cash and Cash Equivalents	18.056	47.254	1.243.985	78.934	1.559.628	68.426
Pfd Eqty & Mnrty Int	0	0	0	0	0	0
Sales	63.396	95.623	1.023.586	885.042	680.578	148.464
EBITDA	4.973	12.692	369.604	125.525	316.799	-10.240
EBIT	3.975	10.344	253.162	95.773	249.144	-13.044

Exhibit 22: Estimation of Market Share in Instant Messaging, Pre-Merger (European Commission 2011)

IM Provider	Market shares June 2011 EEA-wide
Facebook	[50-60] %
WLM	[30-40] %
ICQ	[5-10] %
Skype	[0-5] %
Yahoo! Messenger	[0-5] %
Ebuddy.com	[0-5] %
Google Talk	[0-5] %

Exhibit 23: Estimation of Market Share in Video Calls, Pre- and Post-Merger (European Commission 2011)

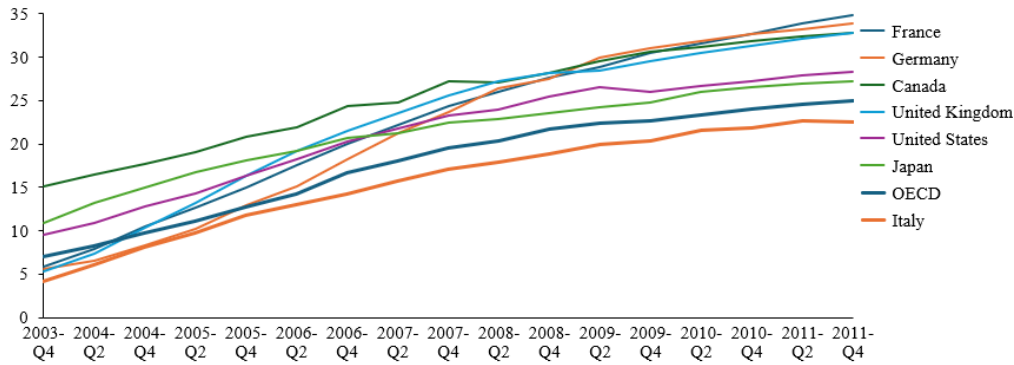
Video Call Provider	Market shares June 2011 EEA-wide	Post-merger EEA-wide market shares
Skype	[40-50] %	[80-90] %
WLM	[30-40] %	
Facebook	[5-10] %	[5-10] %
ICQ	[5-10] %	[5-10] %
Yahoo!	[0-5] %	[0-5] %
ooVoo.com	[0-5] %	[0-5] %
Google	[0-5] %	[0-5] %
AOL	[0-5] %	[0-5] %

Exhibit 24: Cost of setting up a competing Service (European Commission 2011)

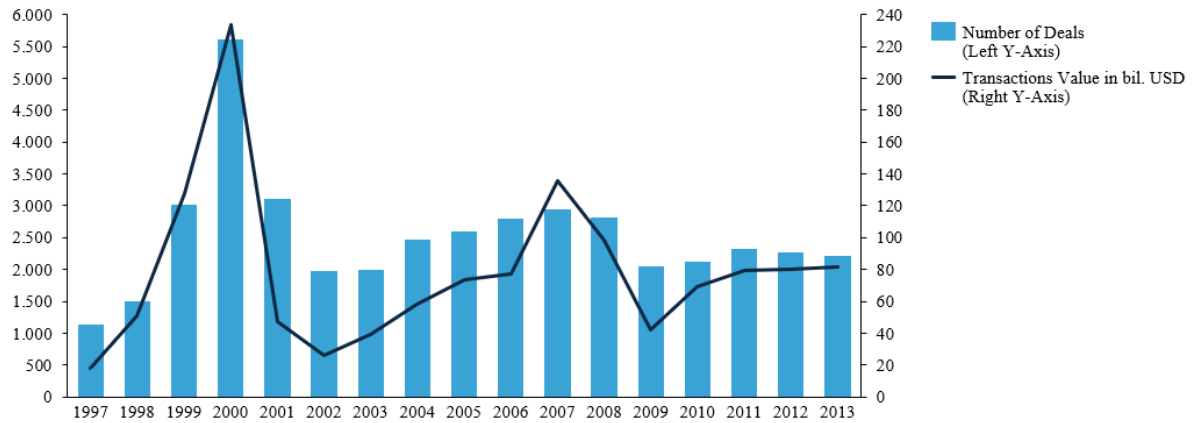
Capital Investment	EUR 0.75 – EUR 9.7 million
Estimated time to market	8 – 24 months
Number of users one year after launch	2.4 million – 17 million

Appendix

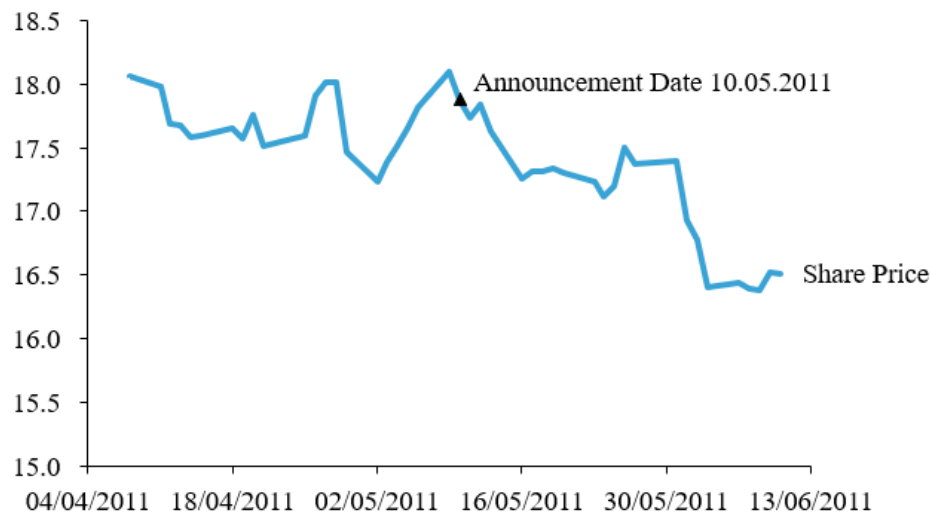
Appendix 1: Historical fixed broadband penetration rate of the G7, 2003-2012 (OECD 2003-2012)



Appendix 2: Software & Internet Services M&A deal number and transaction volumes, 1997-2013 (Institute for Mergers, Acquisitions & Alliances 1997-2013)

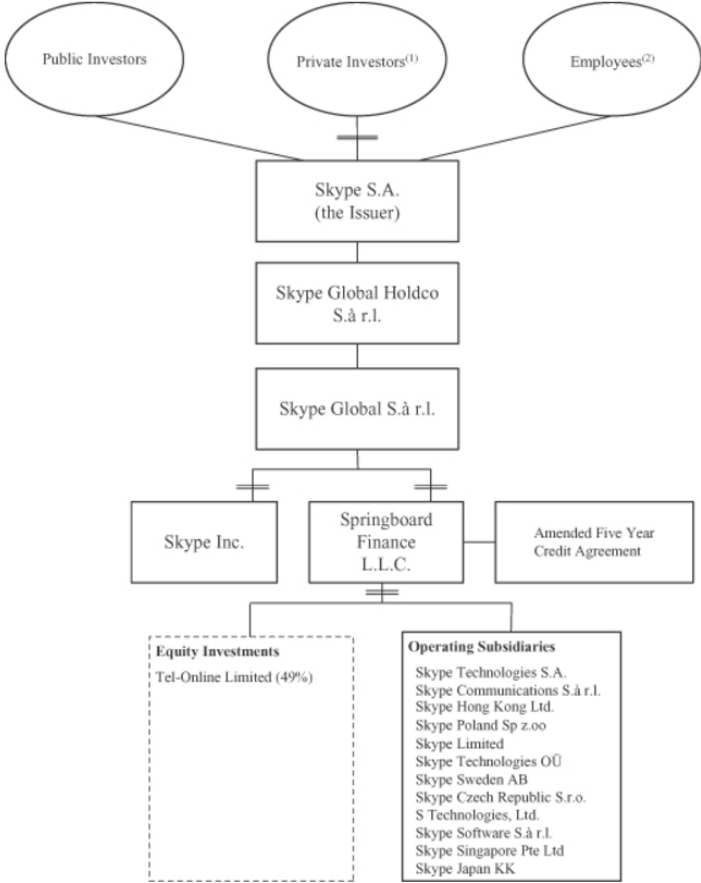


Appendix 3: Microsoft Stock Price one Month prior and one Month post Announcement (S&P Capital IQ)



Appendix 4: Skype Shareholder Structure prior to the Microsoft Merger (Skype S.à.r.l. 2010)

GENERAL PART



⁽¹⁾ Includes Silver Lake, CPP Investment Board Private Holdings Inc., Andreessen Horowitz, eBay, Joltid, Charleston Investment Holdings Limited and certain of their affiliates. See "Principal and Selling Shareholders."

⁽²⁾ Prior to this offering, employees, directors and consultants who invested in Skype Global or who acquired ordinary shares pursuant to the exercise of any stock option granted under the Skype Equity Incentive Plan held their equity interest in Skype Global through Skype Management, L.P. ("Skype Management"), an exempted limited partnership organized under the laws of the Cayman Islands, which is a shareholder in Skype Global, primarily to enable Skype Global to comply with the limitation on the number of record holders of its ordinary shares under applicable law. Skype Management received such acquired shares on behalf of the employees, directors and consultants and issued a corresponding number of partnership units to the employees, directors and consultants. In connection with this offering, the partnership will terminate and be wound up and Skype Management's ordinary shares in Skype Global will be distributed to the employees, directors and consultants according to their respective numbers of partnership units.

INDIVIDUAL PART – SIMON HUSCAVA

viii. *Regulatory Approval and Cisco Challenge*

a. Introduction

Back then Microsoft's largest acquisition to date, the merger of Microsoft and Skype represented a noteworthy consolidation in the tech sector drawing significant public attention. Amid fears of killer acquisitions stifling innovation the EC made a controversial antitrust decision which was not left uncontested.

Timeline:

- 10/05/2011 Microsoft announces Skype deal
- 17/06/2011 Approval issued by the FTC
- 02/09/2011 Notification of the European Commission
- 07/10/2011 Approval issued by the European Commission
- 13/10/2011 Consummation of Merger
- 16/02/2012 Cisco challenges the European Commission's approval of the merger
- 11/12/2013 General Court of the European Union rejects the challenge

b. Learning Objectives

Throughout the preparation of the case study, students will:

- Analyze the merger approval of the EC and appreciate the multifaceted view, beyond market shares, required to judge this unique case from an antitrust perspective.

- Evaluate Cisco’s challenge of the ruling to recognize how different stakeholders might try to modify the outcome of a merger.
- Apply the concept of killer acquisitions to this business combination to acknowledge contemporary challenges of evolving antitrust approaches.

At the end, students will be challenged to answer **why the deal was approved initially and whether the Cisco challenge was a credible threat to the merger.**

c. Teaching Plan

The following teaching plan is recommended for the instructor’s use:

- Familiarize the students with antitrust processes and requirements in the EU and US
- Give background on relevant market dynamics and conglomerate effects assessment to help understand why the deal was approved.
- Discuss how and why different agents could try to influence a merger outcome via the Cisco challenge and a brief theoretical excursus to hell-or-high water clauses.
- Introduce the concept of killer acquisitions.

d. Antitrust Requirements

To introduce the case and initiate a discussion, the instructor is encouraged to test the knowledge of the students about the aspects antitrust authorities might pay attention to to appraise the market impact of a deal. A sample of potential answers can be found in Appendix 4 of the teaching note. The additional information in Appendix 4 will bring valuable context to appreciate subsequent sections but is not essential to the case. Depending on how familiar the students are with the deal, at this point, the discussion can be taken further by collecting arguments for and against an antitrust approval of the merger on the whiteboard (Exhibit 12,

Teaching Note). This may be revisited at a later stage when students spent more time working on the case.

e. European Commission Decision

Taking on the role of an external legal counsel to Microsoft, students are expected to evaluate why the EC approved the deal initially. Subsequent sections provide the instructor with mitigating arguments and reasoning by the EC for its decision.

1. Instant Messaging

Students are expected to deduce that at the time of the merger Skype was not a significant player in the IM market and thus the merger would not significantly change market share. The IM market was highly dynamic as illustrated by Facebook, amassing a 50% market share in less than three years while WLM lost users in the two years leading up to the merger (European Commission 2011). An additional mitigant of potential harm to competition students might come up with was the growing use of smartphones and tablets where WLM was mostly absent. With messaging services increasingly integrated into free social networks such as Facebook with low switching costs, it is unlikely that Skype would have been able to charge for the service or stop innovating.

2. Voice Calls

As WLM held a relatively low market share in voice calls, the combination would have resulted in a combined market share equivalent to Skype's pre-merger market share. Moreover, also in this segment, WLM users decreased rapidly by [10-20] % worldwide between March 2011 and May 2011. An additional argument would be the fierce competition in the VoIP space as well as of traditional telecom, public switched telephone network (PSTN) providers. In 2010, Google entered into the voice calls segment offering PSTN calls for free in the US and for competitive fares in the EEA, underbidding Skype (European Commission 2011).

3. Video Calls

Despite creating a clear market leader in the video calls segment the European Commission greenlit the deal. This decision was underlined with data by Skype stating that over 75% of its users would switch to an alternative service if they started charging money for video calls (European Commission 2011). Due to the low switching costs, similarly, users might have switched platforms if Skype stopped innovating which was crucial to its growth in the past. Also, in this segment WLM faces declining user numbers, among other reasons, due to their limited presence on tablets and smartphones as well as strong competitors such as Google and Facebook as well as many new market entrants including Bistri, IMO Instant messaging and Friendcaller (European Commission 2011).

4. Enterprise Communications Services

The parties submitted that Skype should not be considered as a participant in the enterprise communications market as its client lacks a lot of the collaboration functionalities such as calendar, email and joint documents, typically present in such software. The client is the same for consumers and businesses and it was estimated that only [5-10]% of Skype users do so exclusively for business purposes, mostly SMEs. In the most narrow market considered, IM, voice and video calls for businesses, excluding other services, the merger would not have formed a dominant player. Further mitigating factors were plentiful competition by, i.a. Citrix, Adobe and Intercall as well as the fast growth in the sector (European Commission 2011).

5. Conglomerate Assessment

When evaluating potential conglomerate effects students are expected to recognize that Microsoft's vast product range, complementary to Skype, as well as strong position in OS (Windows), internet browsers (Internet Explorer) as well as office suite bore the potential for conglomerate effects. Microsoft would have been able to degrade Skype's compatibility with

operating systems other than windows, integrate it into Windows or bundle it commercially with its Office suite.

To assess conglomerate effects, the EU's "Non-horizontal Merger Guidelines" requires an evaluation of the ability and an incentive to foreclose and whether there would be a likely negative impact on competition and consumers (European Commission 2011).

Students are expected to recognize that Microsoft clearly had the ability to engage in the above-mentioned practices i.e. had the ability to foreclose. However, students should recognize that there was little incentive to do so since Skype's value is closely tied to its user base. Reducing the interoperability of Skype products on other platforms would lead to a loss of users and thus degradation of the Skype brand and investment value as well as advantage for competitors offering services on platforms other than Windows. With healthy competition available offering similar services free of charge, Skype is not a must-have service. As has been established, Skype estimated that a large number of users (~75%) would switch if Skype started charging money for its free services. Therefore, Microsoft had a clear incentive to keep Skype mostly free and maintain the Skype brand across platforms. The same arguments highlight how there was little to no incentive to engage in bundling or tying of Skype to Microsoft products. Moreover, above reasoning highlights that, even if Microsoft would have pursued a degradation of interoperability or bundling the potential harm to consumers and competition would have been negligible (European Commission 2011).

Regarding the conglomerate assessment of the merger in the context of the enterprise communications market, the European Commission addressed concerns by competitors such as degradation of interoperability or bundling. It was ultimately concluded that such concerns existed independently of the merger due to the (not market-leading) position of Lync but with no relation to the tie-up with Skype. Such concerns were thus not relevant to the merger review.

The EC relatively quickly, within the first review period, deemed the tie-up to be compatible with the internal market of the EU and allowed the merger to go ahead.

The following list of standard questions is proposed. The instructor is free to modify them as they please:

- After examining the characteristics of the consumer and enterprise communications market, how do you believe the Microsoft Skype deal would impact competitors and consumers?
- What mitigating factors led the EC to approve the merger in spite of high combined market shares in certain market segments?
- Do you believe Microsoft could likely benefit from conglomerate effects?
- How could different stakeholders try to modify the deal outcome or manage antitrust rejection risk?

f. Managing Antitrust Risk

At this stage, the instructor is invited to make an excursus to introduce students to contractual ways of managing antitrust risk. This may serve as a discussion starter for further ways and motives for the attempted modification of merger outcomes by different stakeholders leading to the Cisco challenge.

Although there is no publicly available information on clauses contained in the Microsoft – Skype merger agreement, it is possible that the contract contained mechanisms to preclude regulatory rejections. In such clauses regulatory approval as conditions precedent to closing of the transaction is negotiated. They may differ in language ranging from “reasonable effort” to “any and all actions necessary” which would be called a “hell-or-high water” clause. Such a clause would require full compliance with conditions set by the regulator such as divestures of

other business segments. This can be mitigated via a “material adverse effects” (MAE) clause stating that any and all necessary actions have to be taken unless it would have a material adverse effect on the business. The negotiation between parties revolves around allocation of antitrust risk where the seller would usually push for stricter, hell-or-high water type clauses to secure the purchase consideration while the buyer would want to minimize their obligations. The use and structure of such a clause might shed more light on the perceived antitrust rejection risk by the merging parties. (quinn emanuel trial lawyers 2022)

g. Cisco Challenge

Students are tasked to provide Microsoft with an evaluation of the risk stemming from Cisco’s challenge to the deal approval. With the available information as well as additional research students are expected to deduce why the challenge was unsuccessful and recognize what other motives Cisco might have had for its challenge.

After ruling that the application for annulment of the merger was admissible, the General Court of the European Union (2013) established that, contrary to the argumentation of the applicants, merger regulation foresees an assessment of probabilities and regulators do not need to prove that a concentration would not give rise to any competition concerns. Furthermore, it was determined that the EC does not have to address all arguments brought forward by stakeholders in the fact-finding process and has some level of discretion regarding the extent of its analysis due to time and resource constraints.

With regards to the high combined market share in consumer video communications on Windows PCs the court reiterates the arguments brought forth in the initial ruling and notes that the applicants failed to establish the existence of such a narrow market which, for the purpose of analysis represented a “worst-case scenario”. It was stressed that competitive pressure from communications software on other platforms or devices was still present and relevant. This line

of argumentation can teach students that regulator's considerations of market shares in very narrow potential market overlaps, in the eye of the law, do not have to equate to market power (General Court of the European Union 2013).

The court also stated that even if the alleged market power in video calls on Windows PC were true, the contestants failed to present evidence how this market power would enable the combined entity to harm competition since no video call platform operator thus far has been able to charge for the service (General Court of the European Union 2013).

Concerning the complaint about network effects, the court found that Cisco and Messagenet failed to bring forth arguments or evidence of network effects in video communications and also did not establish how network effects would impact competition in the segment of video calls on Windows PCs. Also, the complaint that the EC did not prove capacity to switch services was rejected since the original EC decision contained information proving that users tend to be present on multiple platforms (General Court of the European Union 2013). The complaint regarding harm to innovation was also dismissed since, as affirmed in the original decision, innovation is a key driver of consumer communications services and customers would have been easily able to switch platforms should Microsoft have attempted to deprive Skype of innovation (General Court of the European Union 2013). Cisco's complaint about potential preferential interoperability between Skype and Lync giving the combined entity a business advantage. The applicants failed to explain why business users on Lync would want to communicate with Skype users which are almost entirely consumers. Neither ability nor incentive for such strategy was reasonably proven (General Court of the European Union 2013). What can be taken away from the above paragraphs is that a successful challenge of an EC merger ruling would require more tangible evidence to either credibly discredit conclusions made in the assessment or bring forth evidence that the Commission failed to address an important concern. Furthermore, a reasonably likely impediment to effective competition

would need to be proven. What the overall ruling shows is that Cisco and Messagenet did not bring forward a particularly strong case for annulment of the merger as all complaints were rejected by the court. Students might recognize how, beyond achieving an outright block, delaying the merger or achieving the imposition of conditions such as a restriction on foreclosure could have been reasons for Cisco to undertake such a challenge.

The approximate blocking rate by the EC of 0.27% between 2013 and 2022 also underlines how rare an outright block of a merger is in the EU (European Commission 2013-2022). In the majority of cases, the court sides with the EC, not having overturned a ruling since 2002 (Reuters 2013).

The following list of standard questions is proposed. The instructor is free to modify them as they please:

- What additional arguments could Cisco have brought forth in their challenge to the decision of the EC to strengthen their case?
- How should such a challenge be framed? What would Cisco need to prove for a successful challenge?
- What could have been additional motives for Cisco to challenge the merger?
- Do you believe the merger agreement contained a hell-or-high water clause?

h. Killer Acquisition

When tasked with evaluating whether the acquisition of Skype by Microsoft could qualify as a killer acquisition students should receive credit for arguments in both directions since research suggests that killer acquisitions are notoriously hard to identify, also by regulators. Especially for nascent firms, it is hard to predict whether the target firm's projects would have created competitive pressure independently (Cunningham, Ederer, and Ma 2021). Hovenkamp (2021)

notes how it is hard to distinguish whether an acquisition is motivated by innovation suppression or legitimate business expansion as there does not tend to be clear evidence of intent. The paper also argues that products or services might be shut down post-merger after the acquirer has made an effort to put the assets to productive use but failed suggesting that, even post-merger, it might be difficult to distinguish failed strategic mergers from killer acquisitions.

Students will likely bring forth similar arguments to those presented in the previous section about the conglomerate assessment. Given the high purchase price, and little overlap in most segments, there was no clear incentive for Microsoft to purchase Skype and stunt its growth and innovation or simply shut it down to pre-empt competition, also because Skype's value was closely tied to its user base as well as freemium business model. There was plentiful competition making it easy for users to switch the service should innovation stop. The quote by Steve Ballmer which was also named in the EU decision provides a public statement opposing this idea. Students might argue that the pace of innovation of the combined entity might have been slower than with both standalone businesses, but such conclusion would be speculative. Students are encouraged to bring forth arguments favoring and opposing the idea. Nevertheless, the takeaway should be either that the evidence is inconclusive to make a definitive judgment or that the concept is not fitting since there is a missing incentive for Microsoft to shut down Skype which would make the motive of a killer acquisition unlikely. This section will familiarize students with the concept of killer acquisitions and give an insight into how antitrust regulation is evolving and what challenges might be associated with new legislation.

The following list of standard questions is proposed. The instructor is free to modify them as they please:

- Could this deal be considered a killer acquisition? Bring forth arguments supporting and opposing this idea.
- Do you believe regulators should be able to challenge any deal, regardless of scope? What might be potential consequences?

i. Epilogue

After the challenge was rejected, Cisco elected not to appeal to the European Court of Justice. Thus, finally the antitrust compliance of the Microsoft – Skype deal was confirmed, and the deal was not modified ex-post. These clear victories for Microsoft highlight the focus regulators put on demonstrable consumer harm as opposed to potential competitive disadvantages to individual rivals.

ix. Epilogue

After Microsoft acquired Skype in 2011 for \$8.5 billion, the platform initially thrived. Skype saw rapid integration into Microsoft's services, replacing Windows Live Messenger by 2013 and becoming a key feature in Office 365, Xbox, and Windows devices. It remained a leading communication tool for personal and business use during its early years under Microsoft. However, competition soon emerged, notably from Zoom and Slack- Furthermore, Microsoft Teams, launched in 2017, began to overshadow Skype. Teams' success, especially during the COVID-19 pandemic, relegated Skype to a less central role (Novet 2023). While Skype remains available, its market share and relevance have significantly declined as Microsoft shifted its focus to Teams for enterprise and collaborative communication (French 2020).

Whether Microsoft's acquisition of Skype was worth it at all and if so, whether the astronomical price tag was justified, remains debated. Initially, the deal appeared successful, as Skype integrated into windows and replaced Messenger, gaining millions of users. Microsoft likely derived some strategic value, particularly through Teams' success, which incorporated lessons from Skype. Despite that, the acquisition is often viewed as overvalued given the high price not justified by common valuation methods as well as Skype's fading prominence (French 2020).

Exhibits

Exhibit 1: Board Plan for the Merger Motives of both Parties

Merger motives of Microsoft	Merger motives of Skype
<ul style="list-style-type: none"> Achieving synergies through tax considerations and savings Enhancing Microsoft's communication technology position by killing a competing technology and preventing the acquisition by other competitors Integrating Skype into Microsoft's already existing division structure and product and service lines (strategic alliances) Leveraging Skype's user base Strategic importance of voice and video communication 	<ul style="list-style-type: none"> Profit Realization Strategic Focus Legacy Considerations Market Conditions

Exhibit 2: Relationship between Skype and Microsoft's Products and Services (Shan 2013)



Exhibit 3: Skype Valuation History (own calculation)

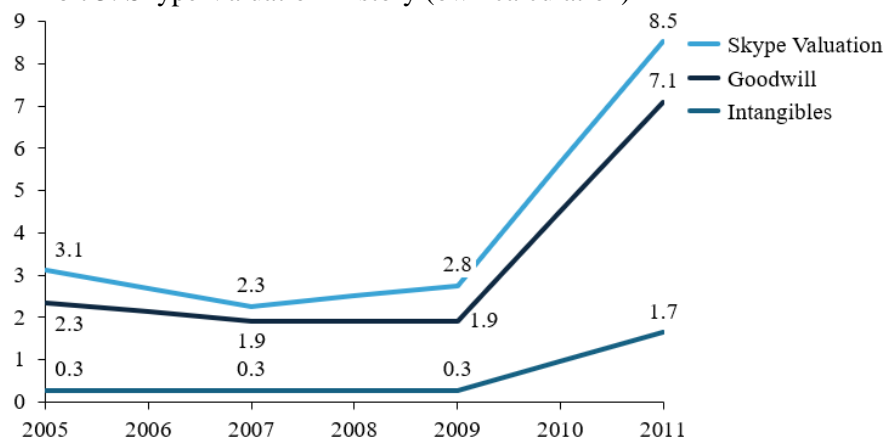


Exhibit 4: Skype Comparable Companies, 2010 (S&P Capital IQ)

Comparable Companies	Company Description	Exclusion Criteria
8x8 Inc.	A VoIP and cloud communications provider with a subscription-based model, directly comparable to Skype's core business.	Included
BroadSoft Inc.	A provider of software solutions enabling telecom service providers to offer VoIP and unified communication services.	Included
Akamai Technologies Inc.	A global leader in content delivery networks (CDN) and cloud services	Size and Industry
Vonage Holdings Corp.	A consumer and business-focused VoIP provider, with a subscription-based revenue model similar to Skype.	Included
VeriSign Inc.	A provider of domain name registry services and internet security solutions	Size and Industry
ShoreTel Inc.	A company specializing in business-focused unified communication solutions	Included

Exhibit 5: Football Field Chart

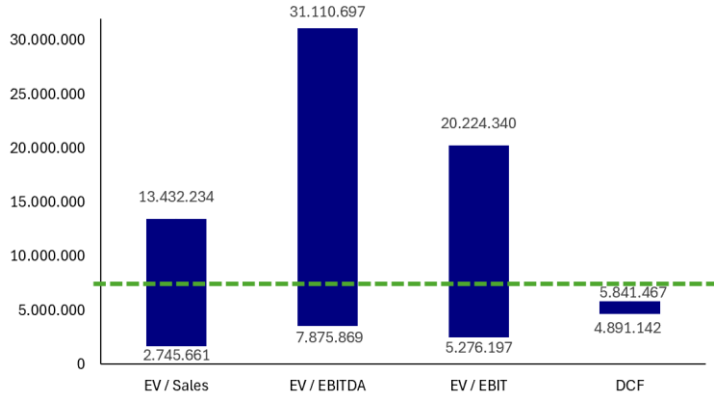
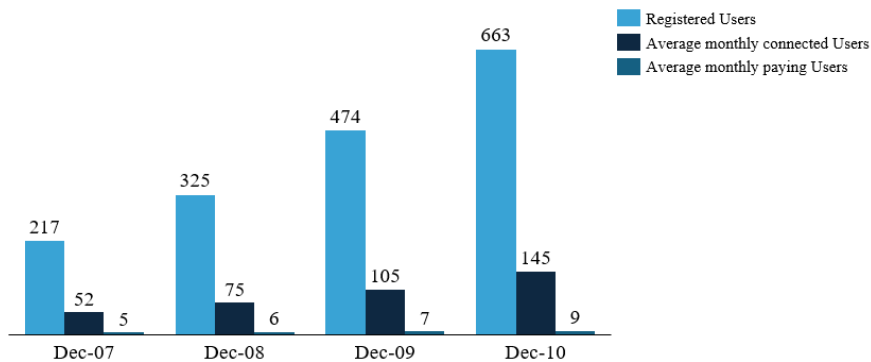


Exhibit 12: Board Plan with Arguments for and against a Merger Approval from a Regulatory Standpoint

Arguments for an approval	Arguments against an approval
<ul style="list-style-type: none"> Nascent and highly dynamic market Market shares are of the narrowest product market with the biggest overlap (Consumer Communications Services on Windows PCs) Microsoft committed to maintain accessibility and interoperability of Skype Low barriers to entry Many potent competitors Low switching costs Services mostly free of charge Shift to smartphones and tablets which were barely addressed by WLM 	<ul style="list-style-type: none"> High combined market shares in certain overlapping segments Integration into Windows OS could reduce interoperability Bundling with existing Microsoft products could reduce consumer choice Strong network effects of Skype's large existing users base and Microsoft resources Potential kill acquisition of competitor Reduced innovation

Appendix

Appendix 1: Skype User Metrics in Millions (Shan 2013)



Appendix 2: Merger Decision Pros & Cons List

Pros	Cons
Large User Base: Skype had over 660 million users, giving Microsoft access to a massive, global audience.	Integration Challenges: Skype's peer-to-peer architecture might clash with Microsoft's centralized cloud infrastructure.
Synergies with Existing Microsoft Products: Skype could be integrated into Office, Windows, and Xbox, improving collaboration and productivity.	Competition in VoIP Market: Despite the acquisition, Microsoft faces competition from Google Voice, FaceTime, and Zoom.
Strengthening Presence in VoIP Market: The acquisition allows Microsoft to enter the growing VoIP market, competing with Google and Apple.	Risk of Overpayment (Hubris): Suffering from the "winner's curse" there is always a risk of overpayment
Defensive Move Against Competitors: Microsoft blocks Google and Facebook from acquiring Skype, protecting its position in communications.	Revenue Model Limitations: Skype struggled to monetize its largely free user base in the past.
Enterprise Communication Enhancement: Skype technology has the ability to boost Microsoft's enterprise communication platform, rebranded as Skype for Business.	Shifting Market Dynamics: Skype lost market leadership to competitors like WhatsApp, FaceTime, and Zoom.
Global Brand Recognition: Skype's strong global brand adds credibility to Microsoft's product portfolio.	Missed Mobile Opportunities: Skype's mobile apps were slow to develop compared to WhatsApp and FaceTime
Boost for Cloud and Mobile: Skype can help Microsoft expand its cloud services and support mobile platforms.	Cultural and Organizational Fit Issues: Skype's integration into Microsoft's corporate structure faces challenges, eventually hindering innovation.
Tax Efficiency: Microsoft can use offshore cash reserves to make the acquisition, minimizing tax costs.	
Increased Use in Remote Work and Education: Skype is a key tool for remote communication during the rise of remote work.	
Monetization Potential: Skype was seen as a platform with strong monetization potential through ads and premium subscriptions	

Appendix 3: Post-Acquisition Structure of Microsoft (Mc Guinness 2011)



Appendix 4: Scope and Process of Antitrust investigations in the United States and European Union

	EU	USA
Scope	<p>Combined aggregate worldwide turnover >€5bn and turnover of each merging party of >€250mn in the EU. Exception when two thirds of combined turnover of both parties is realized in one and the same member state</p> <p>Or</p> <p>Combined aggregate worldwide turnover >€2,5bn and combined EU wide turnover of >€100mn across at least three member states (at least >25mn in each) and EU wide turnover of each party must exceed €100mn</p> <p>If the above rules do not apply the merger could still be subject to approval of national member state authorities</p> <p>(Bundeskartellamt 2004)</p>	<p>Thresholds of deal values subject to antitrust clearance are updated yearly based on GDP changes.</p> <p>In 2011 all mergers with a transaction value >USD 68.2mn required a filing with the Federal Trade Commission (FTC) and Department of Justice (DOJ)</p> <p>Transactions with a value below USD 272.8mn additionally required specific size thresholds of merging parties</p> <p>(Bass, Berry and Sims 2011)</p>
Process	<p>Notification and merger filing including financial and market information with European Commission</p> <p>Phase I review within 25 working days</p> <p>If more concerns arise a Phase II investigation taking up to 90 additional working days can be initiated</p> <p>Decision to approve, approve with conditions or block the merger which the European Commission can decide unilaterally</p> <p>(European Commission 2024a)</p>	<p>Based on Hart-Scott-Rodino (HSR) act of 1976</p> <p>Filings with FTC and DOJ which must include financial and market data</p> <p>Waiting period (typically 30 days)</p> <p>Possibility of Second Request for more detailed information</p> <p>Decision to approve, approve with conditions or file a lawsuit in federal court to try and block the merger</p> <p>(Federal Trade Commission 2013)</p>

Litigation	<p>Appeals of decisions can be made to the General Court of the European Union which conducts a thorough review. Appealing party needs to prove a procedural factual or legal error</p> <p>(European Commission 2024a)</p>	<p>Decisions can be appealed through court litigation leading to a de novo review of evidence and arguments by both parties</p> <p>(Federal Trade Commission 2013)</p>
Appraisal of market impact (non-exhaustive selection)	<ul style="list-style-type: none"> • Market definition • Market position (40-50% market share considered dominant) • Available alternatives • Entry barriers to new entrants • Supply and demand trends for relevant services • Interests of customers (price, choice, quality and innovation) • Efficiencies are considered but must directly benefit consumers • Development of technical and economic progress • Is one party a failing firm <p>(European Commission 2004)</p>	<ul style="list-style-type: none"> • Market definition not always required • Market concentration • Entry barriers to new entrants • Pricing power and ability to reduce quality • Would the merger facilitate collusion among remaining firms • Efficiency gains (innovation, cost savings, etc.) that could offset competitive harm • Is one party a failing firm <p>(U.S. Department of Justice and the Federal Trade Commission 2010)</p>
Key Consideration	<p>Would the merger significantly impede effective competition in the European Economic Area?</p> <p>(SIEC Test)</p> <p>(European Commission 2004)</p>	<p>Does the merger substantially lessen competition?</p> <p>(SLC Test)</p> <p>(U.S. Department of Justice and the Federal Trade Commission 2010)</p>

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