UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

UNITED STATES OF AMERICA,

Plaintiff,

v.

H&R BLOCK, INC.;
2SS HOLDINGS, INC.; and
TA IX L.P.,

Defendants.

Civil Action No. 11-00948 (BAH)

PLAINTIFF'S PROPOSED FINDINGS OF FACT

REDACTED VERSION FOR PUBLIC FILING*

*The United States files this non-confidential redacted version pursuant to the Protective Order entered on June 15, 2011.

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I. INTRODUCTION

1. Last year, approximately 140 million Americans filed their tax returns with the Internal Revenue Service ("IRS"). Tax returns may be filed in one of three ways: (1) unassisted ("pen and paper," which includes preparation by hand and with free fillable electronic forms available on the IRS website); (2) using digital do-it-yourself tax preparation products ("DDIY"); or (3) with assistance from a tax professional ("assisted"). GX 629 at 10-11. DDIY is becoming increasingly popular — an estimated 35 to 40 million taxpayers used DDIY in 2010. GX 19 at 3.

2. Intuit (the maker of "TurboTax"), H&R Block, Inc. ("HRB"), and TaxACT collectively control approximately 90% of the DDIY market — Intuit with 62.2%, HRB with 15.6%, and TaxACT with 12.8%. GX 27. The proposed acquisition would combine HRB and TaxACT, and result in an effective duopoly, in which the next nearest competitor will have a 3 percent share, and most other competitors will have less than a 1 percent share. GX 27.

3. DDIY products are offered through three channels: (1) online through an internet browser; (2) software for a personal computer downloaded from an Internet website; and (3) software for a personal computer on a disc, which is either sent directly to the consumer or purchased by the consumer from a third-party retailer. GX 629 at 11.

II. BACKGROUND

A. Merging Parties

4. HRB is a Missouri corporation with its principal place of business in Kansas City, Missouri. GX 133 at ¶ 9.

5. HRB offers assisted tax preparation services and DDIY products through separate business units, with separate leaders and separate marketing strategies. GX 12 at 1; Bennett, TT,

9/6/11 a.m., 106:2-25.[1] HRB offers DDIY products for consumers under the brand name H&R Block At Home (formerly TaxCut). GX 629 at 9.

6. In 2011, HRB's DDIY products generated approximately [redacted] in revenue. GX 296-2. For the same period, HRB sold approximately 6.6 million DDIY units to consumers. GX 296-2. Separately, in 2011, HRB's assisted business generated approximately $2.7 billion in revenue (based on 14,756,000 U.S. returns at an average fee of $182.96, as reported in HRB's 2011 Annual Report). GX 532 at 32:19-33:1 (Cobb Dep.); GX 565 at 19.

7. 2SS Holdings, Inc. ("2SS") is a Delaware corporation with its principal place of business in Cedar Rapids, Iowa. GX 133 at ¶ 10.

8. 2SS owns 2nd Story Software, Inc., which offers DDIY products under the brand name "TaxACT." GX 629 at 8-9.

9. In the fiscal year ending April 30, 2011, TaxACT products generated approximately [redacted] in net sales and service revenue. GX 151 at 6. In the same year, consumers used TaxACT to electronically file approximately 5 million federal tax returns. GX 151 at 3-4.

10. TA Associates Management, L.P. ("TA") is a private equity firm organized under the laws of Delaware with its headquarters in Boston, Massachusetts. GX 133 at ¶ 11.

11. In December of 2004, TA purchased a majority interest in 2SS for $85 million, and as a result TA has majority control of 2SS Holdings and 2nd Story Software. GX 55 at 72:6-73:4 (Greif Dep.); GX 28-3.

B. The Transaction

12. On October 13, 2010, HRB entered into a merger agreement with 2SS and TA. GX 120 at 1. Under this agreement, HRB would acquire control of 2SS for $287.5 million. GX

[1] "TT" designates trial testimony.

120 at 6; GX 119 at 1.

III. THE RELEVANT PRODUCT MARKET IS DDIY

13. The overwhelming weight of the evidence establishes that DDIY products comprise the relevant market for analyzing the competitive effects of this transaction. This evidence includes: (1) the nature of the products at issue; (2) Defendants' admissions and ordinary course business documents recognizing that DDIY is a separate market in which Defendants and Intuit compete directly and vigorously with each other; (3) the relative pricing of the products at issue and the fact that competitors in the DDIY market generally set their prices without reference to products outside the market; and (4) the testimony of Plaintiff's expert, Dr. Frederick Warren-Boulton, who applied standard economic analysis, including the application of the hypothetical monopolist test, to show that a monopolist of DDIY products could likely impose a small but significant increase in price in the DDIY market.

14. Defendants' argument that the relevant market should include all methods of tax preparation is not supported by the evidence or by credible economic analysis. While it is true that certain documents refer in general terms to competition among various forms of tax preparation, specific references to actual competition among firms overwhelmingly distinguish between separate markets for assisted preparation and DDIY, and identify TaxACT, HRB and Intuit as principal competitors. The testimony of Defendants' executives, who attempted to support a broader market, was generally (1) inconsistent with their own documents and prior submissions to the Justice Department ("DOJ"), (2) illogical, and (3) and without record support. The testimony of Defendants' expert, Dr. Meyer, that assisted preparation is a closer substitute for certain DDIY products than other DDIY products, was based primarily on a "pricing simulator" that she did not prepare or apply and which provides no basis for her conclusions.

A. The Nature Of The Products

15. DDIY and assisted tax preparation are fundamentally different forms of tax preparation products. Assisted tax preparation involves face-to-face human interaction between a taxpayer and a trained tax professional, who reviews or completes tax returns for the taxpayer. DDIY, on the other hand, is a way for a taxpayer to prepare a tax return without any assistance from a tax professional. Instead, the taxpayer uses a software program to guide the taxpayer through a series of steps necessary to complete a return. Once the user completes the steps proscribed by the program, the program's tax engine calculates and prepares the relevant tax forms and schedules for filing. Ernst, TT, 9/7/11 a.m., 32:13-18; GX 294 (Simone Dep. 57:13-19). This step-by-step software program "takes the mystery of those forms out" and allows taxpayers to prepare their returns without having to understand the tax code, know which forms to file, or understand how to complete them. Ernst, TT, 9/7/11 a.m., 33:4-17; GX 572 at 31:20-32:10 (Ernst Dep.); Dunn, TT, 9/8/11 a.m., 47:15-17.

16. As Plaintiff's expert Dr. Rick Warren-Boulton testified, many taxpayers appear to prefer, for various reasons, one form of preparation to the other and do not consider them to be substitutes. Warren-Boulton, TT, 9/9/11 p.m., 60:8-16, 94:22-95:23, 99:19-101:16; *see also* GX 812 at HRB-DOJ-00155385 (HRB admission that "DIYers are different clients; they are unlikely to move across channels."). This conclusion is supported by (1) data showing that the share of assisted tax preparation as a percentage of all filings has remained essentially constant over the last decade, despite a substantial increase in DDIY usage; (2) admissions in Defendants' documents and the testimony of their executives, as well as other evidence, that much of the movement between assisted and DDIY is the result of changes in life circumstances leading to more or less complexity in a tax return; and (3) the substantial price difference between assisted

and DDIY products (discussed in more detail below). HRB is the only significant DDIY competitor which also provides assisted tax preparation products, but it manages these two units as separate businesses, with separate managers and business strategies. In submissions to the DOJ filed just three months before trial, HRB asserted that its assisted business does not compete with its digital business. GX 629 at 92. And, HRB has even sued Intuit for false advertising when it suggested that digital and assisted methods of preparation were comparable. GX 248 at ¶ 30; *see also* Docket #80, IRS Stip. at ¶ 11 (In the context of founding the Free File Alliance ("FFA"), the IRS recognized that DDIY offerings were not comparable to the services provided by an accounting or legal tax professional.). These facts make clear that HRB recognizes a fundamental difference in the nature of the assisted and DDIY products.

17. Defendants' insistence that "pen-and-paper" should be included in the relevant market cannot be taken seriously for several reasons. First, as Defendants' fact and expert witnesses admitted, pen-and-paper is not a product. It is simply the description of the task of completing a tax return by hand, without using assisted or DDIY products. There are no competitors that sell pen-and-paper and the task itself does not involve any economic exchange. Bennett, TT, 9/6/11 a.m., 117:8-19. Meyer, TT, 9/11/11 a.m., 64:21-24; 66:8-22.

18. Second, even if the task of completing a tax return could be considered a "product" in the same sense as DDIY or assisted preparation, pen-and-paper is fundamentally different from both. It requires that an individual taxpayer complete a tax return without any software or human assistance. The taxpayer is on his or her own to understand the relevant provisions of the tax code and to complete the forms. GX 571 at 156:20-157:6 (Petz Dep.); GX 570 at 43:14-20 (On-Line Taxes Dep.); GX 293 at 190:19-24 (Intuit Dep.). Indeed, Defendants recognize that pen-and-paper is a much more complicated, time-consuming, and error-prone

process than using DDIY or assisted products. GX 125 at 6; GX 294 at 58:20-59:13 (Simone Dep.); Dunn, TT, 9/8/11 a.m., 54:23-55:19; *see* GX 293 at 190:12-17 (Intuit Dep.).[2]

19. Third, Defendants recognize that pen-and-paper is not a product by itself, but a pool of potential customers for both their DDIY and assisted products. This pool is rapidly shrinking as taxpayers move principally to DDIY. Indeed, the movement is a one-way street: DDIY has expanded as the number of taxpayers using pen-and-paper has declined. Few taxpayers switch *to* pen-and-paper *from* DDIY. HRB estimates that [redacted] percent of customers who switched away from DDIY in FY10 went to pen-and-paper. GX 128 at 21. IRS tracking found that the number of customers who switched from e-filing to pen-and-paper was "insignificant." GX 569 at 28:22-29:11 (DuMars Dep.).

20. The large and consistent migration of taxpayers from pen-and-paper to DDIY indicates that pen-and-paper does not pose a competitive constraint on DDIY.[3] And this is confirmed by the Defendants' common sense admission that the price of DDIY products is not constrained by pen-and-paper. HRB has not set the prices of its DDIY products based on competition with pen-and-paper, Ernst, TT, 9/7/11 a.m., 31:14-24; GX 61 at 62:3-4 (Houseworth Apr. 8 Dep.), nor has it adjusted the quality of its DDIY products in response to pen-and-paper. Ernst, 9/07/11 a.m., 31:25-32:5. And two former HRB CEOs confirmed that an increase in the price of DDIY products would not cause any significant switching to pen-and-paper. *Id*. at 31:5-

[2] Paper returns have an error rate of around thirty-five percent compared to around five percent for e-filed returns. GX 297 at 35:10-17 (Mamo Dep.); s*ee also* Docket #80, IRS Stip. at ¶ 11 (In the context of founding the FFA, the IRS noted that, regardless of the vehicle used, e-filed returns had a lower error rate than paper returns.).

[3] The use of DDIY products has consistently grown at the expense of pen-and-paper. GX 21-29 at 8; Dunn,TT,9/8/11 a.m. (Public Tr.) 46:11-14; GX 61 at 35:13-36:1 (Houseworth Dep.); GX 296-3A at 8. According to a TaxACT offering memorandum, over a five-year period ending in April 2010, the number of e-filers using DDIY tax preparation products increased at a combined annual growth rate of 14.3%, while, conversely, from tax year 2003 to 2008, the number of pen-and-paper tax filings declined at an 11% annual rate. GX 55-3 at 7. Pen-and-paper's share of all tax returns fell from 16% in FY03 to less than 6% in FY10. GX 128 at 8.

13, 32:6-8; Bennett, TT, 9/6/11 a.m., 119:22-120:1; *see also* GX 572 at 89:13-25 (Ernst Dep.).[4]

21. DDIY firms do not perceive the free fillable tax forms available on the IRS website to be a competing product. GX 293 at 37:21-38:2 (Intuit Dep.); GX 571 at 157:7-17 (Petz Dep.). Free fillable forms merely allow users to enter their data into tax forms online. They lack the guided process available in DDIY products. Ernst, TT, 9/7/11 a.m., 32:9-33:3. Users of free fillable forms must understand and navigate the tax forms on their own. For that reason, only a very small percentage of taxpayers have chosen to use free fillable forms.

B. Defendants' Documents Recognize A Distinct DDIY Market

22. Defendants' documents and testimony show that, for the better part of a decade, they viewed themselves as competing with one another in a distinct DDIY market. Indeed, even as HRB was analyzing the effects of its proposed acquisition of TaxACT in presentations for its senior executives and Board members, it focused principally on a "digital market." In these documents, HRB identified the acquisition as an opportunity to grow its digital "market share" by acquiring a "digital tax competitor." GX 296-18 at HRB-DOJ-00346591. In fact, as part of its acquisition due diligence, HRB measured TaxACT's market share in a single DDIY market with all other DDIY providers. GX 130 at 98.

23. Several of the HRB employees with responsibility to analyze the effects of the transaction highlighted its potential to increase HRB's position in the digital market. HRB's CIO, Mr. Agar, stated the "bottom line" of the TaxACT deal is that "we are stronger together, versus competing and losing share in a growing category," by which he meant the DDIY market. GX 605 at 125:20-126:7, 127:14-16 (Agar Dep.); GX 605-4 at HRB-DOJ-00012402. The head of HRB's digital business, Mr. Houseworth, reviewed a consultant's presentation of

[4] Similarly, TaxSlayer stated that it does "not believe any of TaxSlayer's customers would switch to pen-and-paper [even if TaxSlayer raised its prices a material amount] . . . ." Rhodes, 9/12/11 A.M., 101:24-102:5.

possible post-acquisition strategies (including the elimination of TaxACT as a competitor to HRB) and concluded that the presentation "provide[d] a great context of the Digital market." GX 296-9. Similarly, HRB's Director of Reporting and Corporate Analytics, Mr. Newkirk, noted that HRB and TaxACT combined "would have 29% market share versus Intuit's 54%. Still definitely number two, but there is no other way we could take such a big leap forward in terms of share." GX 21-37 at HRB-DOJ-00355055; Newkirk, TT, 9/7/11 a.m., 96:8-21.

24. Indeed, as recently as September 1, 2011, Mr. Cobb, HRB's current CEO, admitted in statements to the investment community that "[c]ombining H&R Block and TaxACT will . . . bring competition to a *digital market* that's currently dominated by one player, Intuit." GX 1150 at 2 (emphasis added); Cobb, TT, 9/19/11 a.m., 77:17-78:8.

25. These admissions in connection with the proposed acquisition are consistent with how Defendants have described, tracked and analyzed the market for many years. HRB has long HRB tracked digital competitor activity separately from its retail competition, GX 372 at 1; GX 28-10 at 15,17; GX 28-19, and it has commissioned competitive monitoring reports that analyze a distinct digital market and identify Intuit and TaxACT as HRB's competitors in that market. GX 118 at 1,11,16, 23.

26. Similarly, TaxACT creates "Competitive Analyses" that include spreadsheets with detailed comparisons of TaxACT, HRB, and Intuit's respective DDIY products. GX 295-16 at 2SS-KINJe-0001704. TaxACT currently describes itself on its web site as one of the "Goliaths" in the DDIY market, GX 55-5, and acknowledges that the other two Goliaths are HRB and Intuit. GX 55 at 65:20-66:16 (Grief Dep.). When Ms. Grief, TaxACT's co-founder and Chief Marketing Offer, said that 2nd Story Software "is now #2 in the online tax market, sandwiched between two very large, billion dollar companies," GX 55-6 at 2SS-GRECe-

0030506, she was referring to HRB and Intuit. GX 55 at 171:20-172:6 (Greif Dep.).

C. Defendants Admit That They Directly Compete Against Each Other And Intuit

27. There is no doubt that Defendants view themselves and Intuit as the HRB internal documents reference them — the "big 3" digital competitors. GX 61-3 at 5; GX 61-4 at HRB-DOJ-00298625. HRB documents from 2005 through 2011 consistently identify TaxACT as a strong digital competitor. GX 127-4 (TurboTax and TaxACT HRB's most significant competitors); GX 70 (HRB's "Only real direct competitors are turbotax in san diego and TaxACT in cedar rapids"); GX 21-18 at HRB-DOJ-00155594 (TaxACT is "a very serious competitor in the online space"); GX 21-17 (TaxACT is "definitely a serious competitor"); GX 164 at 5 (TaxACT's competitive position: "#3 in the overall digital market and #2 in the high growth online segment"); GX 23 at HRB-DOJ-00347837 (TurboTax and TaxACT and HRB comprise "big three"); GX 296-17 at HRB-DOJ-50266506 (HRB's "two rivals" are TurboTax and TaxACT); GX 61-8 at 1 (TurboTax and TaxACT identified as HRB's main rivals); GX 294 at 140:20-22 (Simone Dep.); GX 531 at 119:8-10 (Ciaramitaro Dep.) (HRB and TaxACT compete outside the FFA).

28. Likewise, TaxACT documents repeatedly identify HRB as one of its primary competitors in its DDIY business. GX 28-32 at 2SS-KINJ-0001261, 64 (HRB is a "major competitor[]" of TaxACT's); GX 7 at 14 (TaxACT's products "equal or superior to either those of Intuit or H&R Block"); GX 102 (TurboTax and TaxCut "direct" competitors); GX 28-8 at 14 (TurboTax and HRB "major competitors"); Dunn, TT, 9/7/11 p.m. (Public Tr.), 93:13-21 (same). In a glossy press kit signed by its CEO, TaxACT identified HRB as one of its two major DDIY competitors. GX 28-10 at 16-17; GX 55-12; GX 55-13. TaxACT has annually prepared an end-of-season competitive analysis that compares only TaxACT, Intuit and HRB, and it did so again

in 2010. GX 55 at 137:4-138:10, 263:1-6, 283:1-284:9, 285:6-12 (Greif Dep.); GX 55-23. Similarly, a June 2010 document that was reviewing the "current competitive landscape" analyzed TaxACT's brand against specifically defined "major competitors" HRB and Intuit. GX 28-32 at 2SS-KINJ-0001263-65; Dunn, TT, 9/7/11 p.m. (Public Tr.), 94:9-14.[5]

D. Defendants Respond To Their Digital Competitors In Setting Prices And Product Features

29. Defendants view one another as digital competitors despite the price difference in some of their offerings. Ernst, TT, 9/7/11 a.m., 21:18-23; Dunn, TT, 9/7/11 p.m., 98:4-9, 99:14-100:6, 105:15-106:3; GX 28-8 at 2SS-CORPe-0025301, 2SS-CORPe-0025313; GX 134 at 2SS-CORPe-001851. Accordingly, HRB reviews TaxACT's and other digital competitors' prices when setting its DDIY prices. GX 127 at 127:6-21 (Bennett Dep.); GX 127 at 126:16-17; GX 188; GX 199. Mr. Newkirk routinely monitored the DDIY prices of TaxACT and Intuit, and was never asked to monitor the prices of any other firm or tax preparation method by anyone except HRB's lawyers in this action. GX 21 at 134:13-20, 135:4-16 (Newkirk Dep. Vol. 1).

30. Beyond observing TaxACT's prices, HRB has cut, or considered cutting its price, in response to TaxACT. In 2009, HRB lowered the price of its "premium" retail software product from $69.99 to $49.99 in order to "better compete with online free," the DDIY product TaxACT pioneered. GX 53 at 2. [redacted] GX 510. In 2010, HRB expressed concern about losing more customers to TaxACT if HRB did not cut its price. GX 53 at 8. As described in more detail in Section V.C. below, competition with TaxACT has impacted HRB's strategy for free products (such as what forms to offer) and has HRB considering [redacted]

[5] TaxACT began to include firms other than TaxACT, HRB, and Intuit in its price comparison documents in December 2010, after HRB announced its acquisition of TaxACT and after the United States began its investigation and issued requests for information to HRB and TaxACT. GX 55-26 at 2SS-MARKe-0017599; GX 55 at 286:8-16, 288:1-3 (Greif Dep.) (including comparison of TaxACT, HRB, Intuit, and TaxSlayer).

[redacted]

31. Similarly, in its day-to-day operations, TaxACT monitors the prices of HRB's DDIY products, as well as those of Intuit. Dunn, TT, 9/7/11 p.m. (Public Tr.), 110:25-111:3; GX 187 at 16; GX 108; GX 265; GX 28-14; GX 28-19 at TA00088; Dunn, TT, 9/8/11 a.m. (Public Tr.), 9:13-19; GX 28-35; GX 28 at 187:18-188:2 (Dunn Dep.); GX 200; GX 169. TaxACT monitors and considers HRB's and Intuit's prices because TaxACT has to differentiate itself from those two firms through, among other things, its lower prices. Dunn, TT, 9/7/11 p.m. (Public Tr.), 100:21-102:19; GX 28 at 235:13-19 (Dunn Dep.); GX 28-20. And, TaxACT specifically considers the pricing of HRB and Intuit products when setting its prices. GX 295 at 185:3-21 (Kintzel Dep.). Indeed, when TaxACT increased its prices, it purposely kept them below HRB and TurboTax's prices. GX 28-20. *See also* Dunn, TT, 9/8/11 a.m. (Public Tr.), 12:4-13:2 (TaxACT, HRB, and Intuit compete against each other on price).

32. Likewise, when setting its DDIY prices, Intuit looks primarily at the pricing of HRB and TaxACT, in part because those are the other firms with the highest market share in the DDIY category. GX 293 at 194:5-194:8, 194:18-195:8. For its part, TaxACT has run advertisements that compare TaxACT's price to TurboTax's price. GTX 8; GX 959; Dunn, TT, 9/8/11 a.m. (Public Tr.), 25:18-27:2. Such advertisements are an example of price competition between TaxACT and TurboTax. Dunn, TT, 9/8/11 a.m. (Public Tr.), 12:21-13:2.

33. HRB and TaxACT also have similar advertising messages and market to customers in the same way. GX 294 at 122:1-123:2, 207:7-22 (Simone Dep.); GX 61 at 38:20-39:2 (Houseworth Dep.). In part, this is because HRB and TaxACT [redacted]

[redacted] Both use advertising to target each other in an effort to compete. GX 295 at 82:8-19 (Kintzel Dep.); GX 28 at 99:7-17, 203:20-204:3, 210:20-21 (Dunn Dep.); Dunn, TT, 9/7/11 p.m. (Public Tr.), 88:3-23; GX 84 at 30; GX 170. HRB has specifically targeted TaxACT customers to switch to HRB products. Ernst, TT, 9/7/11 a.m., 14:14-17; GX 127-5; GX 5; GX 89; GX 66; GX 76. In 2008, HRB's Vice President of Marketing for its digital division recommended increasing its online advertising "[i]f we are going to compete aggressively against TaxAct and the 'others.'" GX 82; *see also* GX 83 at 21; GX 84 at 30; GX 85; GX 86; GX 87; GX 88 at 25.

34. Similarly, TaxACT [redacted]. GX 109 at 2SS-MARKe-0012718. For example, TaxACT has bid on the paid search keywords [redacted] GX 28-25 at 3; GX 55 at 180:8-17, 181:3-11, 181:19-182:4, 244:9-245:5 (Greif Dep.); GX 55-17. Ms. Greif testified that TaxACT bids for search terms containing the names [redacted] GX 55 at 182:19-183:22 (Greif Dep.). Dr. Warren-Boulton's analysis of TaxACT's advertising shows that when TaxACT increased its advertising in select metropolitan areas, its sales in those areas increased compared to areas where it did not advertise. At the same time, HRB's digital sales in those same areas declined compared to areas where TaxACT did not advertise. Warren-Boulton, 9/9/11 A.M., 18:12-20; GX 234 at 15.

35. TaxACT's ability to develop low priced digital products and market them effectively forced HRB to improve its product quality in order to better compete. GX 28 at

167:14-168:5; GX 293 at 163:10-18; GX 293 at 189:8-11. For example, in 2007, HRB prepared a "TS08 Digital Tax Solutions Product Brief" that compared HRB DDIY product features with those of TaxACT and Intuit. GX 127-6. And, in 2008, HRB's analysis of its TaxCut products compared its products with those of Intuit and TaxACT. GX 127-19. Similarly, in 2009, TaxACT's "Competitive Analysis TY 2009" focused solely on competition in the market for DDIY products and analyzes competition solely among TaxACT, HRB, and Intuit. GX 104. Competition with HRB and TurboTax was driving changes in TaxACT's messaging, product quality, and strategy. *Id*. HRB also changed its product offerings when it determined its products were not competitive, including its login process. Ernst, TT, 9/7/11 a.m., 19:1-25, 22:9-23:2; GX 93; GX 127-6 at 7-8.

36. TaxACT considered [redacted] GX 28-18 at 2SS-CORPe-0027845. When HRB and Intuit offered maximum refund guarantees that would return the purchase price if the customer obtained a better result with another DDIY product, TaxACT responded to the competition by offering its own improved maximum refund guarantee that would even provide a payment to any user of TaxACT's free product. GX 55 at 254:1-255:6 (Greif Dep.).

E. Assisted Tax Preparation Is Not In The Relevant Market

37. The record does not support Defendants' contention that assisted tax preparation is in the same product market as DDIY. To the contrary, Defendants admitted in a joint statement submitted to the DOJ on May 2, 2011 that that HRB "recognize[s] that the digital tax preparation business serves do-it-yourself customers and does not adversely affect its much larger assisted tax preparation business." GX 629 at 92. This admission alone is sufficient to reject Defendants' contentions regarding assisted tax preparation.

38. There are, however, substantial additional admissions by Defendants and other evidence demonstrating that assisted tax preparation and DDIY are not in the same market. One of the most compelling facts is that none of the principal DDIY competitors sets its prices in relation to prices for assisted products. [redacted] GX 295 at 186:9-16 (Kintzel Dep.), HRB sets the prices of its digital and assisted products separately, GX 572 at 57:13-23 (Ernst Dep.); Ernst, TT, 9/7/11 a.m., 35:4-6, [redacted][6]

39. Indeed, DDIY firms generally recognize that assisted products do not constrain their product pricing because of the significant price disparities between the two. GX 293 at 18:17-21 (Intuit Dep.); GX 607 at 80:20-23 (Liberty Dep.); GX 28-6; Dunn, TT, 9/8/11 a.m., 54:23-55:23. For example, the average price of TurboTax, the most popular DDIY product, is approximately $55. GX 296-7 at 6. The average price of HRB's DDIY product is approximately $25. GX 296-7. The current DDIY industry average price is $44.13. GX 121 at 57. In contrast, the average price of an assisted tax return is in the range of $150-$200. GX 293 at 21:9-14 (Intuit Dep.); Bennett, TT, 9/6/11 p.m., 100:6-23.[7]

40. There are numerous high level HRB documents recognizing separate DDIY and assisted markets and identifying different competitors in each market. For example, a June 2010 presentation to the HRB Board distinguished between the assisted and DDIY markets,

[6] Similarly, neither TaxSlayer nor TaxHawk consider the prices charged by CPAs or tax stores when setting the prices of their DDIY products. Kimber, TT, 9/12/11 a m., 48:16-20. Rhodes, TT, 9/12/11 a m., 101:8-11.

[7] Liberty Tax, a company with both retail tax stores and a DDIY product, charges, on the low end, $160 in its tax stores. GX 607 at 51:10 (Liberty Dep.). In contrast, the high end cost of Liberty's DDIY product is $80. GX 607 at 51:11-18 (Liberty Dep.).

identifying only Intuit and TaxACT as competitors under "Digital Competitor Analysis." GX 492 at 8,12. An HRB presentation to Moody's Investor Service in October 2010 similarly described a separate "competitive landscape" for the DDIY and assisted markets. GX 127-21 at 9. And two former HRB CEOs testified that DDIY does not compete with assisted products. Bennett, TT, 9/6/11 a.m., 108:2-109:18; Bennett, TT, 9/6/11, p.m., 91:22-92:6; Ernst, TT, 9/7/11 a.m., 33:18-34:19.

41. The fact that Intuit apparently has made efforts to attract assisted customers to its digital products does provide a sufficient factual basis to conclude, as Defendants allege, that assisted and digital products are in the same market. First, HRB failed to call an Intuit witness who could provide direct evidence of the extent and success (if any) of any Intuit's marketing efforts directed at assisted customers. Second, an HRB document in the record indicates that Intuit's efforts may not have been successful. GX 1151 at 16 (citing Intuit executive and noting that Intuit failed to take share from tax stores.). Third, despite Intuit's attacks on HRB's tax stores, HRB's former CEO, Mr. Ernst, who subsequently served in a senior IRS position, did not view its digital business as competing with HRB's assisted business. Ernst, TT, 9/7/11 a.m., 33:18-34:19. [redacted] And, fifth, as Dr. Warren-Boulton explained, the fact that Intuit may attempt to attract to customers from assisted does not mean that assisted and digital are in the same market; standard economic principles do not require that all diversion occur within the relevant product market — the relevant issue is the nature of the diversion within the relevant market. Warren-Boulton, TT, 9/20/11 a.m., 5:20-6:12.

42. Other industry characteristics support Plaintiff's view that assisted and DDIY are not in the same market, including the nature of switching between assisted and DDIY. The

primary reason consumers shift from DDIY to assisted tax preparation is changes in life circumstances that increase the complexity of an individual's tax returns. Ernst, TT, 9/7/11 a.m., 34:20-35:3; Bennett, TT, 9/6/11 a.m., 110:7-19; Bennett, TT, 9/6/11, p.m., 54:5-15; GX 127-2 at 6; GX 126 at 15; GX 204 at HRB-DOJ-00138116; GX 28 at 15:15-18, 193:2-4 (Dunn Dep.); Dunn, TT, 9/8/11 a.m., 47:19-48:20, 94:12-14; GX 607 at 30:8-19, 80:4-8 (Liberty Dep.); Warren-Boulton, TT, 9/20/11 a.m., 7:1-6; Dunn, TT, 9/7/11 p.m., 76:4-15 (the reason a customer would switch to assisted from tax software is because the customer lost confidence in tax software or because of a change in life circumstances.).

43. In a Market Dynamics analysis, HRB concluded that the "main reason for switching to HRB retail is due to more complex tax returns" and "*[i]ncreased* complexity is the most frequently cited reasons for switching from Paid Family/Friends and DDIY methods (P&P, Software, and Online)." GX 128 at 30-31 (emphasis in original). HRB found that [redacted] of customers who switched from HRB offices to online cited "Tax return less complex" as their primary reason. This was the second most cited reason behind [redacted] at [redacted]. GX 128 at 32. Among customers switching to HRB offices, [redacted] coming from online and [redacted] coming from software cited "Tax return more complex" as their primary reason. Only [redacted] of the online and none of the software respondents cited [redacted] GX 128 at 30. HRB has estimated that [redacted] of software users and [redacted] of online users that switched to HRB paid preparation stores [redacted] GX 635 at 30. Based on these studies, it is not surprising that HRB's former CEO Russ Smyth stated at an investor conference that "the choice of digital versus retail as a tax preparation alternative is not an economic one." GX 1358 at 30.

44. In addition, there has been significant growth in the DDIY market, while, at the same time, the assisted market has remained static, even when the prices for DDIY products

have increased. GX 128 at 9, 38. Similarly, as the relative price of assisted products has risen, the relative market share of assisted tax preparation also increased. GX 121 at 32. As a whole, over the last ten years, there has been very little net movement between DDIY and assisted tax preparation. GX 296-3A at 7.

45. DDIY growth has not been at the expense of assisted. GX 1151 at 4; Cobb, TT, 9/19/11 a.m., 69:3-22; GX 1510 at 2; Bennett, TT, 9/6/11 a.m., 112:19-113:15; Bennett, TT, 9/6/11 p.m., 90:9-14; GX 127 at 98:9-16 (Bennett Dep.); GX 176 at HRB-DOJ-00009740; GX 178 at HRB-DOJ-00193815; GX 179 at 2. According to HRB's TS10 Market Dynamics, "[a]lthough online has been growing, this has not been coming at the expense of assisted…" and "[w]hile online has been growing, the proportion selecting an assisted option has not materially changed. This suggests that *online is not pulling incrementally from assisted*." GX 128 at 9 (emphasis in original); GX 1510 at 2-3. Moreover, HRB did not see a significant change in migration from assisted to DDIY [redacted] GX 813 at HRB-DOJ-00359719; Newkirk, TT, 9/7/11 p.m., 10:2-23; GX 21 at 244:13-245:14 (Newkirk Dep.).

46. The current industry structure, in which there are distinct markets for assisted and DDIY products is not likely to change within the next several years. As Dr. Warren-Boulton explained, the demand for the two products is distinct — many taxpayers appear to prefer one form or the other for reasons having to do with nature of the products and the complexity of their returns. Warren-Boulton, TT, 9/20/11 a.m., 16:3-17:10; Warren-Boulton, TT, 9/9/11 p.m., 60:8-16, 94:22-95:23, 97:23-98:15, 99:19-104:11.

47. While individual taxpayers shift between these markets, there is no evidence that they are doing so because of any perceived similarity between DDIY and assisted. Significantly,

efforts to introduce products that combine features of both markets, so-called hybrid products, have not been successful. HRB has been trying for years to create a "do-it with-me" market, whereby customers could complete their own tax returns with assistance from HRB tax professionals, but such efforts have been unsuccessful, producing poor financial returns. GX 1519A at 14; Warren-Boulton, TT, 9/9/11 p.m., 99:19-100:01; Bennett, TT, 9/6/11, p.m., 28:8-17. For example, HRB calculated that only [redacted] taxpayers purchased the Best of Both product in 2011. Newkirk, TT, 9/7/11 p.m. (Sealed Tr.), 15:18-25, 16:3-18; GX 296-7 at HRB-DOJ-60099526, and [redacted][8]

48. In short, there is no evidence that the development of hybrid products is likely to lead to any blurring of the line between DDIY and assisted markets in the next several years or that any assisted or hybrid products would prevent a hypothetical monopolist from raising the price of DDIY products, which is the relevant question. Warren-Boulton, TT, 9/9/11 p.m., 100:01-101:08.

F. Defendants' Testimony Regarding The Relevant Market Is Not Credible

49. Several of Defendants' trial witnesses attempted to show that all methods of tax preparation compete in a single market, referring to document excerpts that described general tax preparation industry conditions and occasional references to competition within the overall industry. As described above, however, the substantial majority of the evidence makes clear that Defendants for many years have consistently acknowledged a discrete DDIY market and have responded vigorously to each other's price and product competition in this market.

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[8] [redacted]

50. In addition, much of the testimony regarding product markets was not credible. First, the testimony was inconsistent with Defendants' submissions to the DOJ, made just months before trial. While Defendants' witnesses asserted at trial that there is a broad market encompassing all tax preparation methods, Defendants asserted in those submissions that (1) there are much smaller, distinct markets for "value" and "premium" products, GX 135 at 14,15; (2) HRB, Intuit and TaxACT each sell products in those separate markets, GX 135 at 15; and (3) assisted and DDIY do not compete with each other GX 629 at 92.[9]

51. Second, much of the testimony simply did not make sense. For example, TaxACT's CEO, Lance Dunn, tried to distinguish between "value" and "premium" segments, but he could not provide any estimate of market shares for the companies within these alleged segments and acknowledged that there is direct competition between the alleged segments. Dunn, TT, 9/8/11 a.m. (Public Tr.), 50:25-51:8; Dunn, 9/7/11 a.m. (Public Tr.) 58:18-59:3; Dunn, TT, (Public Tr.) 9/7/11 P.M., 62:16-18. Moreover, after first denying that TaxACT prepares competitive analyses tracking prices and product features for Intuit, HRB and TaxACT, Dunn, TT, 9/7/11 p.m., 111:24-112:14, Mr. Dunn admitted the contrary (after being confronted with evidence that such documents had been produced from his own computer files), as well as that these analyses make no distinction between "value" and "premium" segments and do not refer to assisted or pen-and-paper. Dunn, TT, 9/8/11 a.m., 105:22-107:2; GTX 9; GX 28-19.

52. Similarly, while Mr. Cobb, HRB's current CEO, asserted at trial that DDIY and assisted products compete in a single product market, his testimony was not credible in light of the following facts: (1) he became the CEO in May 2011 and had little prior experience in the

[9] After HRB's CEO admitted that the "value" and "premium" segmentation was an "artificial construct," GX 532, at 129:11-130:7 (Cobb Dep.), and Defendants admitted that before the transaction "HRB [did] not consistently use[] the words 'value' and 'premium,'" GX 853 at 13 n.48, Defendants abandoned that argument. At trial, Defendants only argued that value/premium distinction was relevant to the issue of whether the transaction would result in anticompetitive effects.

tax industry, Cobb, TT, 9/19/11 a.m., 61:16-62:4; (2) his testimony was at odds with the deposition testimony of Mr. Houseworth, the current head of HRB's digital business, who admitted that assisted and pen-and-paper do not affect the pricing of HRB's digital products, GX 296 at 89:2-90:1 (Houseworth Dep.) and was not called by HRB as a trial witness, Cobb, TT, 9/19/11 a.m., 62:16-63:2, 80:1-81:19; (3) Mr. Cobb failed during his deposition in August 2011, less than one month before trial, to say whether HRB's digital business competes with its assisted business, despite being asked this questions six times in a row, GX 532 at 54:8-59:6 (Cobb Dep.); and (4) Mr. Cobb told the financial community on September 1, two weeks before his trial testimony, that there is a separate digital market, GX 1150 at 2.

53. Moreover, the weight of the evidence does not support either Mr. Dunn's or Mr. Cobb's suggestion that TaxACT is competing in a separate "value" category. Defendants failed at trial to establish any functional distinction between "value" and "premium" products, or demographic difference between "premium" and "value" customers. GX 295, 8/3/11, 96:1-97:11 (Kintzel Dep.); GX 132 at 18. Defendants admit that all digital providers are competing for the same pool of customers, GX 127 at 115:11-19 (Bennett Dep.); Dunn, TT, 9/7/11 p.m. (Public Tr.), 73:15-74:25; GTX 6, and will take customers from any DDIY company, regardless of whether they are "value" or "premium." GX 127 at 121:4-20, 123:6-19 (Bennett Dep.).

54. Additionally, the notion that HRB's products are premium products is belied by the fact that nearly [redacted] of HRB's returns in the past year [redacted] were processed totally for free — a [redacted] increase over three years. GX 296-7 at 6, s*ee* GX 602 at 3. In addition, HRB's average sales price is not at a "premium level," but rather is between TurboTax's average sales price and TaxACT's average sales price. GX 21-29 at 11; GX 296-16 at 11; GX 293 at 81:19-82:13 (Intuit Dep.). In fact, in 2010, HRB's average price was closer to TaxACT's than Intuit's.

Bennett, TT, 9/6/11, a.m., 48:7-49:2; GX 492 at 11. For those reasons, HRB perceives itself to be in the "murky middle" between TaxACT and TurboTax. GX 51 at 14; GX 163 at 17; GX 173 at 3; GX 174 at 6; GX 61-7 at 14.

G. Plaintiff's Economic Analysis Confirms That DDIY Is A Relevant Product Market

55. Both Plaintiff's expert, Dr. Warren-Boulton, and Defendants' expert, Dr. Meyer, agreed that the Horizontal Merger Guidelines promulgated by the DOJ and the Federal Trade Commission describe the appropriate methodologies for defining the relevant product market. Warren-Boulton, TT, 9/8/11 p.m., 11:15-12:4; Meyer, TT, 9/13/11 a.m., 72:16-73:6. The key tool described in the Guidelines is the "hypothetical monopolist test" (or "SSNIP test"), which has often been applied by courts. The test asks whether a hypothetical monopolist would impose at least a small but significant non-transitory increase in price (SSNIP) on proposed candidate set of products. If enough consumers would continue to buy one of the products in the candidate relevant market, then the hypothetical monopolist would increase price significantly. Warren-Boulton, TT, 9/8/11 p.m., 16:8-19; GX 1451 at 9. On the other hand, if a sufficient number of consumers switch to products outside the candidate market controlled by the hypothetical monopolist, the candidate market needs to be expanded. Warren-Boulton, TT, 9/8/11 p.m., 37:5-25; GX 1451 at 9.

56. Passing the hypothetical monopolist test therefore confirms that the group of products identified as a market is not drawn so narrowly that "even complete elimination of competition within the group would not significantly harm" consumers. GX 1451 at 8. The test confirms that the group of products is worth monopolizing. Warren-Boulton, TT, 9/8/11 p.m., 17:6-11. The Guidelines also state that the relevant market generally is the smallest set of products that pass the hypothetical monopolist test because broader markets (*e.g.*, all liquids) that

satisfy the test typically yield little insight into competitive harms. GX 1451 at 10; Warren-Boulton, TT, 9/9/11 p.m., 101:9-16. Dr. Meyer and Dr. Warren-Boulton also agreed that this "smallest market principle" should be applied. Warren-Boulton, TT, 9/8/11 p.m., 35:19-36:7; Meyer, TT, 9/12/11, p.m., 55:18-20.

57. Dr. Warren-Boulton employed two distinct quantitative analyses in applying the hypothetical monopolist test to the DDIY candidate market. One of the analyses simulated a hypothetical DDIY monopolist. It indicated that such a monopolist would increase prices by far more than the usual 5-10% threshold. The other analysis, which involved a critical loss test, also confirmed that DDIY products are a relevant market. Warren-Boulton, TT, 9/8/11 p.m., 38:8-39:23. Both the merger simulation and critical loss tests are standard economic tools used in merger analysis. Warren-Boulton, TT, 9/9/11 a.m. (Public Tr.), 8:23-25; Warren-Boulton TT, 9/9/11 p.m., 23:9-15.[10]

58. Dr. Meyer criticized several of Dr. Warren-Boulton's assumptions in the application of the hypothetical monopolist test, including his use of an incremental margin. Dr. Meyer, however, did not perform her own hypothetical monopolist test and, as described below, her own opinions were based on seriously flawed reviews of surveys conducted by third parties.[11] Her criticisms, therefore, cannot be credited. Moreover, the incremental margin assumption used by Dr. Warren-Boulton was conservative, and using higher margins as suggested during his cross examination would provide even stronger evidence that DDIY is a

[10] Dr. Meyer criticized Dr. Warren-Boulton's merger simulation for being static and not taking into account the future value of free customers. This criticism is not sound, as Dr. Warren-Boulton directly accounts for the lifetime value of customers by using average revenue as a measure of price in the merger simulation. Warren-Boulton, TT, 9/20/11 a m., 8:8-9:4.

[11] Similarly, Dr. Meyer failed to create or run her own merger simulation model, a standard tool among economists analyzing the effects of a merger on competition, which is relevant both for product market definition and determining competitive harm. Meyer, TT, 9/13/11 a.m., 111:5-18.

relevant market. GX 121 at 34 (Warren-Boulton Report).

59. In fact, Dr. Meyer does not deny that DDIY passes the hypothetical monopolist test. Warren-Boulton TT, 9/20/11 a.m., 4:9. But she declined to apply the test to a DDIY candidate market on the basis that DDIY products are not uniformly closer substitutes for HRB's DDIY product than are aggregates of other means of tax preparation. In doing so, Dr. Meyer neither invoked a principle of economics nor cited scholarly economic literature. Meyer, TT, 9/12/11 p.m., 69:4-14; Meyer, TT, 9/13/11 a.m., 91:4-21. Dr. Warren-Boulton's analysis of diversion, on the other hand, focused on each DDIY firm's products collectively, which preserves an apples-to-apples comparison of diversion estimates. GX 1001. The Guidelines explain that a market expanded beyond a relevant market that is already large enough to pass the hypothetical monopolist test is apt to lead to misleading market shares that mask the potential for harm. GX 1451 at 9-10. The addition of another unnecessary substitute product to an existing relevant market should always pass the hypothetical monopolist test because consumers were ready to pay the price increase already. However that expanded market may offer little insight into the competitive harms posed by the merger (*e.g.*, an all liquids market would provide little insights into a merger between Coke and Pepsi). Warren-Boulton, TT, 9/9/11 p.m., 101:9-16.

60. In applying the hypothetical monopolist test, the question is whether there is sufficient diversion within the candidate market so that a hypothetical monopolist gains more than it loses in raising prices. Dr. Warren-Boulton explained that significant diversion outside the DDIY candidate market would occur but would not prevent the hypothetical monopolist from raising price, thus satisfying the hypothetical monopolist test. Warren-Boulton, TT, 09/20/11 a.m. 5:12-6:12. The Guidelines recognize that a correctly defined relevant market may have significant substitution to products outside of the market. GX 1451 at 9.

61. Although the hypothetical monopolist test could support a somewhat narrower market, Dr. Warren-Boulton conservatively included all DDIY products in the relevant market. Warren-Boulton, TT, 09/8/11 p.m., 36:22-37:7. Importantly, Dr. Warren-Boulton defined each firm in the market as a product, avoiding the "apples-to-oranges" comparison of diversion ratios that plagues Dr. Meyer's analysis. Warren-Boulton, TT, 9/20/11 a.m., 4:15-25. Aggregating many individual firms into a category, such as "assisted," allows Dr. Meyer to add up all the diversion across all the firms in the category. This makes it appear as if HRB consumers are more likely to switch to one product called "assisted" when in fact they are quite unlikely to switch to any particular assisted product.[12] Warren-Boulton, TT, 9/20/11 a.m., 4:14-5:6. Further, since the hypothetical monopolist test has established that there is enough diversion within DDIY for a monopolist to raise price, diversion outside the digital market is irrelevant to that price increase. Warren-Boulton, TT, 9/20/11 a.m., 5:20-6:12.

62. Nor is there any basis, as Dr. Meyer suggests, to question Dr. Warren-Boulton's results because he relied on the IRS switching data, which reveal significant diversion within DDIY, at levels sufficient to confirm the hypothetical monopolist test. Warren-Boulton, TT, 9/20/11 a.m., 5:7-11. IRS data is clearly reliable and are used by the Defendants and other DDIY competitors to track market share.

63. The IRS data reflects real market choices of consumers and not their responses to a hypothetical survey question. Warren-Boulton, TT, 9/20/11 a.m., 9:9-25. Moreover, industry participants saw no reason to think all switching would be much different than switching because

[12] Dr. Warren-Boulton assembled his candidate relevant market by considering which tax preparation products were similar in nature, and the evidence suggested DDIY products were all similar. Warren-Boulton, TT, 9/9/11 p.m., 43:1-5. Dr. Warren-Boulton also tested a "Big-3" market, and found it also passed the Hypothetical Monopolist Test, but chose to define the market more broadly to be conservative." Warren-Boulton, TT, 9/9/11 p.m., 43:4-19; Warren-Boulton, TT, 9/8/11 p.m., 36:18-39:23. While a hypothetical monopolist of Intuit and HRB DDIY products might profitable impose a SSNIP, that market is irrelevant to understand the effects of a merger between HRB and TaxACT. *Id.* at 40:9-24.

of a price change; for example, [redacted]

H. Defendants' Expert Opinion Is Not Credible

64. The quantitative basis for Dr. Meyer's opinion that the relevant market includes all forms of tax preparation consists entirely of her review of two projects undertaken for Defendants by an outside vendor with whom Dr. Meyer is not associated. Meyer, TT, 9/13/11 a.m., 31:9-22, 50:18-22. These projects include (1) a pricing simulation exercise conducted in 2009 for HRB ("Pricing Simulator"), and (2) a 2011 survey undertaken for TaxACT in 2011 solely for the purpose of persuading the DOJ that it should approve the transaction at issue in this case ("2011 Litigation Survey"). Meyer, TT, 9/12/11 a.m., 37:24-38:6, 44:11-16. Specifically, Dr. Meyer claims that the results of these projects provide quantitative evidence of diversion among tax preparation products and that this evidence shows that assisted products and pen-and-paper are closer substitutes for certain DDIY products than other DDIY products. Meyer, TT, 9/13/11 a.m., 38:4-15. Serious methodological flaws render both the Pricing Simulator and the 2011 Litigation Survey unreliable bases for Dr. Meyer's conclusions.

65. Dr. Meyer's reliance on the Pricing Simulator and the 2011 Litigation Survey is particularly suspect both (1) because Defendants failed to call any witnesses who actually participated in the design and conduct of those surveys and (2) because Dr. Meyer did not undertake any independent econometric analysis, or use any of economists' standard tools of merger analysis. Meyer, TT, 9/13/11 a.m., 38:4-15, 89:16-22, 111:7-18.

66. Dr. Meyer did not perform a hypothetical monopolist test on the DDIY market

alleged by Plaintiff, Meyer, TT, 9/13/11 a.m., 73:7-11, nor on her putative product market, Meyer, TT, 9/13/11 a.m., 73:19-23. *See* Warren-Boulton, TT, 9/8/11 p.m. (Public Tr.) 34:20-36:11. Instead, Dr. Meyer testified that a hypothetical monopolist test is “inherent” in her market. Meyer, TT, 9/13/11 a.m., 74:2-13. The SSNIP test is inherent in Dr. Meyer’s market because it is comprised of *all* tax preparation methods. Meyer, TT, 9/13/11 a.m., 77:10-78:1. In other words, in order for a consumer to file her tax return, he or she *must* obtain her tax preparation from Dr. Meyer’s hypothetical monopolist. Accordingly, any monopolist over such a large market could raise prices well beyond 5%-10%. There is simply no other way for consumers to file their tax returns. Meyer, TT, 9/13/11 a.m., 77:10-78:1; Warren-Boulton, TT, 9/8/11 p.m. (Public Tr.), 34:20-36:17.

67. There is no sound methodological basis for starting with a hypothetical monopolist over such a wide range of products that the monopolist can charge an infinite price. Warren-Boulton, TT, 9/08/11 p.m. (Public Tr.), 15:25-17:11, 33:24-36:11. Dr. Meyer’s approach is akin to starting with a product market of “all liquids” rather than determining if “colas” or “sodas” are a market over which a monopolist could impose a SSNIP. Warren-Boulton, TT, 9/9/11 p.m. 99:19-101:16. Her failure to conduct a SSNIP test on a smaller market, such as Plaintiff’s alleged market, is fatal to her market definition. Warren-Boulton, TT, 9/8/11 p.m., 34:20-36:17.

i. The 2011 Litigation Survey Is Unreliable

68. Dr. Meyer relied principally upon the 2011 Litigation Survey to reach her conclusion that TaxACT’s closest competitor is pen and paper. Meyer, TT, 9/15/11 a.m. (Public Tr.), 27:5-22; Meyer, TT, 9/13/11 a.m., 61:10-21. But, the 2011 Litigation Survey does not measure diversion from TaxACT. Indeed, Dr. Meyer concedes that the survey only “sheds some

light" on diversion. Meyer, TT, 9/13/11 a.m., 38:4-10.

69. The 2011 Litigation Survey was not created in the ordinary course of business but was commissioned by TaxACT, HRB, and "legal counsel" to help create evidence to convince the Government that the merger would not harm competition. Meyer, TT, 9/13/11 a.m., 50:18-22; DX 9015 at 1. The fact that the 2011 Litigation Survey was conducted for the explicit purpose of persuading the Government, alone, makes its results highly suspect. GX 624 at 237.

70. The most significant flaw in the survey is that it does not measure diversion, *i.e.*, consumer response to a price change, because the survey does not ask about a price change. Meyer, TT, 9/13/11 a.m., 52:21-23. Dr. Meyer was aware of this significant fact, yet testified in response to the Court's questions that the survey "specifically asked about price change." Meyer, TT, 9/12/11 p.m., 68:7-10. Dr. Meyer subsequently conceded that there is no specific price change indicated, no price range, not even a percentage increase in price. Meyer, TT, 9/13/11 a.m., 52:21-23, 53:10-17, 54:5-18; DX9015 at 1. Accordingly, Dr. Meyer's response to the Court's question about the survey asking about prices wasn't "one hundred percent accurate." Meyer, TT, 9/13/11 a.m., 52:21-53:1. As Dr. Meyer eventually conceded, rather than asking about a price change, the survey asked "[i]f you became dissatisfied with TaxACT's price, functionality or quality, which of these products or services would you have considered using to prepare your federal taxes?" Meyer, TT, 9/13/11 a.m., 53:10-17; DX9015 at 1.

71. Notwithstanding this fatal flaw, Dr. Meyer chose to rely on this survey and to reject surveys that were conducted in the ordinary course of business — even when those ordinary course surveys asked the critical question at issue in the case: how would consumers respond to a price increase. GX 1351 at 38; Meyer, TT, 9/13/11 a.m., 57:13-60:22. One such survey found that a vast majority of respondents would continue using a DDIY product if

TaxACT charged for its free product. *Id*.

72. In April 2008, HRB reported results of a survey of FFA and online free users. Respondents were asked what they would do if their current brand were not free to "you" next year. GX 1351 at 38. Dr. Meyer agreed this survey question specifically involves a price increase. Meyer, TT, 9/13/11 a.m., 58:15-20. According to the HRB business documents summarizing the survey results, approximately 90-95% of respondents would switch to another brand's free online product or would pay a fee to continue to use their current brand. Meyer, 9/13/11 a.m., 59:11-21. These survey results support Plaintiff's relevant product market by showing diversion primarily within the DDIY market.

ii. The Pricing Simulator Used By Defendants' Economic Expert Is Unreliable

73. Dr. Meyer based her conclusions regarding the quantification of consumer diversion from HRB to assisted preparation on a wholly unreliable Pricing Simulator. Meyer, TT, 9/13/11 a.m., 6:4-6. If the Court disregards the Pricing Simulator, there is no other quantitative basis to support Dr. Meyer's view that assisted preparation methods are a closer substitute to HRB than other DDIY products. Meyer, TT, 9/13/11 a.m., 89:17-22. Though the Pricing Simulator is the sole basis for her opinion that "the largest diversion from HRB's TaxCut, in the event of a price increase, is to CPAs and accountants," Meyer, TT, 9/13/11 a.m., 10:20-11:4, Dr. Meyer is unable to specifically identify which TaxCut products she applied the price increase to or the size of the increase applied. Meyer, TT, 9/13/11 A.M., 10:20-12:15.

74. The Pricing Simulator is based upon a consumer survey in which respondents were shown different scenarios where the pricing of some of the products were changed. Meyer, TT, 9/13/11 a.m., 10:2-16; DX 9231 at 3. Dr. Meyer did not conduct the survey or construct the Pricing Simulator herself. Meyer, TT, 9/13/11 a.m., 31:9-12. Survey respondents were asked to

select which of 34 different tax preparation methods they would most likely choose under each of the pricing scenarios. Meyer, TT, 9/13/11 a.m., 24:2-12; DX 9231 at 3.

75. A significant flaw in the Pricing Simulator survey is that 9 of the 34 tax preparation method options presented in the survey were "Non-Priced Choice Options." Meyer, TT, 9/13/11 a.m., 26:10-30:13; 36:19-37:12; DX 9231 at 3-4. Importantly, all of the various subsets of the "assisted" category were "non-priced choice options." Meyer, TT, 9/13/11 a.m., 26:24-27:12; DX 9231 at 3-4. Indeed, the "products" that Dr. Meyer concludes have the most diversion for HRB digital products, namely CPAs and accountants, are "non-priced choice options." Meyer, TT, 9/13/11 a.m., 26:24-27:12, 10:20-11:2; DX 9231 at 3-4.

76. Dr. Meyer has written that a survey is supposed to reflect a "controlled market experiment," reflecting what consumers would do in the event of a price increase. Meyer, TT, 9/13/11 a.m., 9:8-24. But, in the real world, respondents would have known a price for a CPA or accountant before choosing them. Meyer, TT, 9/13/11 a.m., 36:16-18.

77. Dr. Meyer sought to defend the Pricing Simulator survey by claiming respondents did not need to be provided a price because they would each have a price for these products in their own mind. Meyer, TT, 9/13/11 a.m., 28:10-23. Ultimately, Dr. Meyer conceded she did not know what was in the mind of the respondents. Meyer, TT, 9/13/11 a.m., 37:9-12.

78. Another problem with the Pricing Simulator is that the results from the simulator that are captured on the document Dr. Meyer used to calculate her diversion ratio provide a very different diversion ratio depending on which page is used for the calculation — even though all the pages are based on the same pricing simulator data. Meyer, TT, 9/13/11 a.m., 48:18-21; Meyer, TT, 9/15/11 p.m., 62:15-22. Dr. Meyer calculated a 1.6% diversion from HRB TaxCut to TaxACT based on page 18 of DX 9231. Meyer, TT, 9/13/11 a.m., 44:21-45:13; 48:12-17.

But if she had calculated her diversion ratio on page 17 of DX 9231, she would have calculated the same diversion to be 32% — a "very, very different diversion ratio." Meyer, TT, 9/13/11 a.m., 48:12-23, 44:21-48:23. This result suggests two significant issues: (1) the pricing simulator data (which is the basis for both p. 17 and p. 18) is highly flawed, otherwise the diversion ratio would be similar across the entire data set (and thus similar for the data on both p. 17 and p. 18); and (2) Dr. Meyer was not very careful and did not employ a serious critical analysis of the pricing simulator data.

79. Perhaps the most convincing evidence that the Pricing Simulator is flawed or Dr. Meyer's analysis of the simulator is flawed, or both, is that when the price of TaxCut Online is doubled in the pricing simulator (from $14.95 to $29.95) there is absolutely no share change in the share of TurboTax Online Basic (which is among the products that Dr. Meyer testified would receive the highest diversion from HRB's TaxCut). DX 31; Meyer, TT, 9/15/11 p.m., 4:21-7:10. If TurboTax were really one of TaxCut's closest substitutes, economic theory would suggest it would receive a lot of diversion in response to a 100% price increase in TaxCut Basic. Yet, the simulator showed absolutely no change in the share of TurboTax Basic in response to a 100% price increase in TaxCut Basic. DX 31; Meyer, TT, 9/15/11 P.M., 4:21-7:22.

80. Assuming, *arguendo*, that the pricing simulator produced reliable results, the diversion of consumers from HRB digital to the aggregate of all other DDIY products is greater than the diversion to any other product category, such as "assisted." GTX 15. After aggregating both the products offered in the DDIY category and the products offered by the thousands of firms in the "assisted" category, the aggregate diversion ratio is greater to DDIY than to assisted. GTX 15. So, when doing an "apples-to-apples" comparison, there is more switching (or diversion) from HRB digital to DDIY than to any other product. Meyer, TT, 9/13/11 a.m., 93:3-

95:15; GTX 15. Dr. Meyer's aggregation is a fundamental error. Warren-Boulton, TT, 9/20/11 a.m., 4:10-5:6.

IV. THE RELEVANT GEOGRAPHIC MARKET IS WORLDWIDE

81. Joint Pre-Hearing Statement at IX.A., ¶ 12.

V. THE TRANSACTION WILL SUBSTANTIALLY LESSEN COMPETITION AND RESULT IN HIGHER PRICES AND LOWER QUALITY

A. The Merger Will Result In Market Concentration Sufficient To Create A Presumption Of Significant Consumer Harm

82. The proper way to measure market share in the DDIY market is with IRS e-file data, which is both accurate and reflects real market choices. Moreover, this is how Defendants and other industry participants do it. *See, e.g.*, GX 27; GX 21-7, at 3-18; Dunn, TT, 9/8/11 a.m. (Public Tr.), 62:10-18; Dunn, TT, 9/7/11 p.m., 60:24-62:4, 104:16-20, 109:22-25; GX 28, vol. 1 at 32:19-33:11 (Dunn Dep.); Newkirk, TT, 9/7/11 p.m. 5:3-19; GX 21, vol. 1 at 25:6-21, 27:2-9, 85:15-86:6, 126:16-19 (Newkirk Dep.); GX 134 at 2SS-CORPe-001850; Rhodes, TT, 9/12/11 a.m., 97:3-98:14. Indeed, the digital sales figures used to calculate concentration measures in the Complaint come from Defendants' own submission to the DOJ. GX 629 at 11 n.24.

83. There is no need to adjust these figures for state filings since the choice of a federal DDIY provider determines which DDIY provider will be used for state. HRB's study showed that [redacted] GX 600 at 8.

84. The DDIY market is highly concentrated. According to IRS e-file data, Intuit, HRB, and TaxACT collectively control approximately 90% of the DDIY market in 2010 (tax year 2009): Intuit with 62.2%; HRB with 15.6%; and TaxACT with 12.8%. The next two DDIY providers in size, TaxHawk and TaxSlayer each serve about 3% of the market. GX 27.

85. Defendants analyzed this transaction using similar market share figures. For example, HRB's "Project Island Overview, June 10, 2010," which was prepared in connection with the TaxACT acquisition, states that pre-merger, Intuit has 54% of the DDIY market, HRB has 17% of the market, and TaxACT has 14% of the market. GX 493 at 6. Moreover, the head of HRB's digital business, Mr. Houseworth, reviewed the 2010 IRS digital e-file numbers for HRB and its digital competitors and wrote "Check this out – separation of men from the boys is beginning to happen in Online. . . . With TaxACT off the market, all players remaining make up less than 10% in Digital share." GX 21-7 at HRB-DOJ-00012326.

86. The proposed acquisition of TaxACT by HRB produces a post-acquisition HHI of 4,691 with a change in HHI of 400. A change of HHI of 200, to a post-merger market with an HHI of 2500, creates a structural presumption of consumer harm. GX 1001; Warren-Boulton, TT, 9/8/11 p.m., 41:25-42:21. Post-acquisition, HRB and Intuit will control a combined 90% of the DDIY market.

87. The increase in concentration is sufficient to raise a presumption of significant consumer harm absent ease of entry or efficiencies sufficient to offset this harm. Warren-Boulton, TT, 9/8/11 p.m., 19:10-16.

B. Elimination Of TaxACT As An Independent Competitor Will Result In A Unilateral Price Increase

i. A Unilateral Price Increase Is Likely

88. Dr. Warren-Boulton used a merger simulation model to analyze harm. Such models have, for some time, been standard tools of economic analysis. Warren-Boulton, TT, 9/9/11 a.m. (Public Tr.), 9:23-9:25. A merger simulation model requires, as an input, data on diversion across products. Dr. Warren-Boulton relied upon two sources for estimates of diversion, IRS switching data and market share data. Using market share data is the traditional

way economists estimate diversion. Warren-Boulton, TT, 9/20/11 a.m., 10:1-22. The simulation also examines the Defendants' price-cost margin. Higher margins and diversion ratios support large price increases.

89. When a consumer switches tax preparation products, she may do so for reasons other than price: a life event for example, such as a divorce. Thus IRS switching data contains all the consumers who changed products due to price, as well as consumers who changed products due to an increase in the complexity of filing their returns. IRS data show that taxpayers who switch from DDIY to a firm in the assisted category are twice as likely to have an increase in complexity than taxpayers that stayed within DDIY. Warren-Boulton, TT, 9/20/11 a.m., 7:1-12; *see also*, GX 121 at 47. In one run of his simulation, Dr. Warren-Boulton used this fact to better estimate true diversion from the IRS switching data. He discounted consumer switching to assisted from DDIY by one half, and used that as the estimate of diversion in his model. Dr. Warren-Boulton's use of additional IRS information provides a strong basis for this estimation choice. Warren-Boulton, TT, 9/20/11 a.m., 7:1-12. Using his standard merger simulation model and IRS data, Dr. Warren-Boulton estimated diversion between HRB and TaxACT to be 12-14%. Warren-Boulton, TT, 9/20/11 a.m., 10:12-14.

90. Dr. Warren-Boulton's merger simulation model predicted between $16 million and $24 million in annual harm to consumers, solely as a result of the unilateral incentive to increase prices, absent efficiencies. Warren-Boulton, TT, 9/9/11 a.m., 26:5- 18; GX-1003.

91. Plaintiff's expert, Dr. Meyer, did not create or apply her own merger simulation model. Meyer, TT, 9/13/11 a.m., 111:9-18. She claimed that a merger simulation was not appropriate given the amount of free product distributed by the parties, but, Dr. Warren-Boulton explained, there is nothing unusual about this market and merger simulations are routinely

applied in all kinds of markets. Warren-Boulton, TT, 9/19/11 a.m., 8:23-25; *Id.*, 9/20/11 a.m., 8:5-9:4; GX 665 (Warren-Boulton Reply Report) at 14-15. Rather than using her own model, Dr. Meyer used Dr. Warren-Boulton's model, changing some of the inputs, including crediting all efficiencies that Defendants claim. Significantly, when she did this, the model still predicted substantial unilateral effects from the acquisition, resulting in harm of about $2.5 million each year. Meyer, TT, 9/13/11 a.m., 112:23-113:6. Even this figure grossly underestimates the likely harm from the transaction, because, *e.g.*, it relies on the lower bound of diversion estimates from Dr. Warren-Boulton, includes all claimed efficiencies as if they were verifiable and merger-specific, and does not include coordinated effects. Warren-Boulton, TT, 9/20/11 a.m., 10:23-12:1.

ii. The Merger Will Create An Incentive For HRB To Unilaterally Raise Price

92. The merged entity will have the incentive and ability to unilaterally raise price.

93. Today, TaxACT is not motivated to raise price. Bennett, TT, 9/6/11, p.m., 112:6-10. HRB feared TaxACT would continue to grow aggressively at HRB's expense or be acquired by a firm that would help it become even more effective. In October 2009, Mr. Bowen presented to HRB's management team an analysis of the strategic options regarding TaxACT. Bowen, TT, 9/19/11 a.m., 7:25-8:5; DX244. The identified "downsides" of not purchasing TaxACT included "TaxACT continues to grow and HRB loses market share," and "Risk of competitor purchasing TaxACT." *Id.* at 7; GX 61-14 at 7. HRB losing share has obvious negative profit implications for HRB. A competitor purchasing TaxACT could improve the product's features if it chose. Bowen, TT, 9/19/11 a.m., 9:3-22**.** An improved TaxACT would, all else equal, reduce HRB profits as consumers switch away in response to TaxACT's improved value proposition.

94. An acquisition by HRB would change TaxACT's incentives. Before the merger,

TaxACT was simply interested in promoting its low-cost DDIY tax software. By contrast, the merged entity would also want to protect its high price HRB-branded products. Bennett, TT, 9/6/11, p.m., 112:21-25; 114:5-9; *see also* Dunn, TT, 9/8/11 a.m. (Public Tr.) 109:9-24). Because consumers are willing to substitute between the two, the merged entity will want to increase the price of TaxACT and reap profits in increased high-priced HRB sales.

95. HRB could degrade the quality of TaxACT's free product and use it as a marketing tool to attract consumers to HRB. HRB would like to use the TaxACT brand to market free federal and low price products, Bennett 9/06/11, P.M., 88:11-23, but after the merger, HRB will [redacted] GX 55 at 317:16-318:16 (Greif Dep.). [redacted] In other words, it will be harder for consumers to find and use the parties' free products. In contrast, if the TaxACT merger does not consummate, Mr. Houseworth wishes to [redacted]

96. Post-merger, HRB may be less likely to offer a free federal product through TaxACT that is as robust as today. Warren-Boulton, TT, 9/20/11 a.m., 18:7-24. Dr. Meyer similarly indicated in her expert report that post-acquisition HRB will withdraw its low-cost offerings because of concerns that such offerings dilute the HRB brand. DX0017 at 78. Indeed, HRB's stated goal for the transaction is to "migrate TaxCut higher into the segment with less focus on free." GX 172 at 10. Mr. Dunn himself said that the goal of every premium firm is to do everything in its power to get consumers to upgrade from a free product. Dunn, TT, 9/7/11 p.m. (Public Tr.) 69:23-70:5, 70:17-23.

97. As a profit-maximizing firm, HRB post merger will be able to successfully raise price because it will make more money on the customers that it keeps, than it will lose on customers that switch to products that are not controlled by HRB. Warren-Boulton, TT, 9/9/11 a.m., 5:3-8:12. There are two reasons this is true. First, there is substantial diversion between DDIY products, of which two are HRB and TaxACT. Second, the margin earned on each consumer HRB gains from TaxACT is large because TaxACT's average dollar margin ([redacted]) is considerably lower than HRB's ([redacted]). Warren-Boulton, 9/9/11 a.m., 24:4-15; GX 1003.

98. Although the United States is not required to prove the precise mechanism by which a unilateral price increase will be implemented, Defendants have provided some evidence relating to certain possible mechanisms. Moreover, this evidence also shows that anticompetitive effects are being actively contemplated, and are indeed likely. TaxACT made two different recommendations, Plan T and Plan B to HRB regarding the management and marketing of the DDIY products in the merged company. GX 55-31; GX 55 at 317:16-20, 322:2-5 (Greif Dep.). HRB was receptive to both plans, and, as of April 5, 2011, had not yet decided on either of the two recommendations. GX 55 at 326:9-15 (Greif Dep.).

99. One recommendation that TaxACT made to HRB is to [redacted]

[redacted]

100. The other recommendation that TaxACT has made is to [redacted]

101. Dr. Meyer also effectively conceded that DDIY prices are likely to increase due to the merger when she agreed that "TaxACT has been a constraint" on other DDIY providers and that "HRB doesn't want to compete on price." Meyer, TT, 9/15/11 p.m., 10: 9-25.

102. HRB considered another two brand strategy to raise prices. Before the merger, HRB's general strategy was to price its products below Intuit. Bennett, TT, 9/6/11, a.m., 99:7-16. According to the two-brand strategy endorsed by Mr. Bennett, HRB's strategy post-merger would be to price its products equal to or above Intuit, which would result in a five percent or greater price increase. DX 1005-001; Bennett, TT, 9/6/11 a.m., 101:1-102:14, 94:7-11; Bennett, TT, 9/6/11 p.m., 109:15-25; GTX 2. Relatedly, HRB's own candid assessment of the benefits

consumers can expect if the transaction is approved was: "none." GX 16 at 24.

103. Analyses by Intuit confirm that the merger will likely produce significant unilateral anticompetitive harm. [redacted]

C. Elimination Of TaxACT As An Independent Competitor Will Result In Coordinated Effects

i. TaxACT Is The Market Maverick Because It Has Different Incentives Than HRB And Intuit

104. For many years, TaxACT has been a maverick competitor, pricing substantially below HRB and Intuit and introducing innovations such as "free" products that have forced competitive responses from HRB and Intuit. GX 1006 at ¶ 4 (Warren-Boulton Decl.). Dr. Warren-Boulton summarized the history of the DDIY market with a particular focus on two "major disruptive or maverick action," Warren-Boulton, TT, 9/8/11 p.m. 24:13, the offer of free-for-all through the FFA and the free-for-everyone on its website. *Id*. at 21:25-25:19. What characterizes TaxACT's actions as maverick behavior, as opposed to garden variety innovation, is the asymmetry between TaxACT's reasons for its choices and those of its competitors, and therefore, the response the actions evoke from competitors. Here, competitors were "forced to reduce price and provide a better deal to consumers." *Id.* at 30:5-6. Lowering price is the last

thing the seller of a premium branded product would choose to do on its own. But TaxACT, a company without a premium brand to protect, gains enormously from widely offering a free product. Consumers have gained from the maverick behavior because competitors were forced to "come up with a very strong value proposition at the free end." *Id*. at 30:5-6. Since TaxACT's original disruptive conduct in the FFA in tax year 2002, "free" products have become the most popular DDIY products and the inflation-adjusted average price paid by consumers of DDIY products has declined about 10%. GX 1000.

105. TaxACT has engaged in uniquely maverick behavior because, unlike HRB and Intuit, "TaxACT doesn't have a cannibalization problem." Warren-Boulton, TT, 9/09/11 p.m. (Public Tr.), 14:23-15:2. TaxACT has worked to "commoditize" the online market, causing downward pricing pressure and "disruption" in the DDIY marketplace. GX 296-16 at 20-21.

106. TaxACT's value proposition, today, is to offer a high-quality product at a low cost. Dunn, TT, 9/8/11 a.m., 115:11-17. TaxACT does not have significant cannibalization concerns because it earns a smaller dollar margin on its low-priced paid products. GX 1006 at ¶ 5 (Warren-Boulton Decl.).

107. Whereas TaxACT depends on a robust free product strategy, HRB does not have the same strategic imperative to offer such a robust free product. Dunn, 9/7/11 p.m. (Public Tr.), 72:10-73:7. Simply stated, HRB cannot "out free" TaxACT without losing almost all its profit. GX 85. HRB has viewed free online filing as a threat to profitability and there is no lack of internal HRB documents making this point. GX 397 at 7; GX 28 at 70:17-19; GX 127 at 188:15-189:18 (Bennett Dep.); GX 397 at 7; GX 28 at 70:17-19 (Dunn Dep.). HRB has higher-priced premium products whose sales it does not want to cannibalize through a high value free product. Warren-Boulton, TT, 9/8/11 p.m., 31:13-33:16; *see also* GX 304, at 31, 36, 50. According to

Mr. Newkirk, "[t]he current primary competitors have no incentive to drive the market further free." GX 21-31 at HRB-DOJ-00354159. Nonetheless, due to TaxACT's success in the marketplace, HRB has been forced to aggressively market its free digital product. GX 61 at 40:15-41:6 (Houseworth Dep.); GX 296 at 41:10-19 (Houseworth Dep.). HRB has recognized that the growth of free federal was "driven primarily by the growth of TaxACT's Standard and Standard+State," which include free federal, with implications including "[c]ontinued erosion of [p]aid units for middle and lower SKUs." GX 20 at 11.

108. Since HRB began testing a free digital product in 2008, the average sales prices of its software products [redacted] percent from [redacted] to [redacted] while the average sales price of its online products [redacted] percent from [redacted] to [redacted]. Newkirk, TT, 9/7/11 p.m., 18:7-11, 19:16-20:15; GX 296-7. HRB's overall digital revenue per customer, accounting for inflation, [redacted] from [redacted] in FY 2008 to [redacted] in FY 2011, a [redacted]. GX 296-7. And HRB's digital revenue [redacted] from 2008 to 2011 by [redacted] Newkirk, TT, 9/7/11 p.m. (Sealed Tr.), 18:7-11, 37:24-38:3. These [redacted] reflect both the increasing choice of consumers to use the free product, as well as discounts provided to consumers to induce them to purchase the paid product.

109. HRB's average online revenue is $[redacted] while TaxACT's average revenue per client is $[redacted] GX 208 at 6. If HRB were to move to TaxACT's pricing model, HRB would [redacted] in revenue. HRB viewed this as a negative consequence of moving to TaxACT's monetization strategy. GX 605-5 at slide 6; GX 605 at 133:5-141:1 (Agar Dep.).

110. In addition to having more expensive DDIY products, HRB also owns retail tax stores, which are more profitable than its DDIY products. GX 293 at 238:7-13 (Intuit Dep.). Unlike TaxACT, HRB's digital goal is, in part, to "introduce people to the benefits of Assisted

offerings/Tax Professional services" so that it can drive customers to its retail stores when DDIY customers have life events. GX 61-16 at 2. This provides HRB another way to benefit from upselling its free customers; they can be encouraged to go to an HRB store or buy paid DDIY, either of which generates profits for HRB.

ii. TaxACT Has A History Of Maverick Behavior

111. As far back as the early 1990s, Intuit and HRB were the only major DDIY tax preparation companies. Dunn, TT, 9/7/11 p.m. (Public Tr.), 49:22-50:10, 50:25-51:10; 51:11-17**.**

112. Since its founding in 1998, TaxACT has been a pioneer in the DDIY market. *Id.* at 51:24-52:22, 53:6-8. TaxACT rapidly gained market share and brand name recognition by offering a full-feature federal tax preparation product free for use online or as free software that is downloaded to a desktop personal computer. GX 7 at 2; Dunn, TT, 9/7/11 p.m. (Public Tr.), 53:16-24, 65:10-12.

113. TaxACT touted itself as a "maverick," Dunn, TT, 9/7/11 p.m. (Public Tr.), 54:24-55:2; GX 3 at 2SS-GRECe-0028583, and a "catalyst for change in the tax preparation industry . . . . [that] has consistently forced the tax preparation industry to become more competitive, and in doing so [has] forced [its] competitors to change as well." GX 4 at 18. TaxACT "disrupted the digital tax prep market" by offering: (1) a "free-for-all" DDIY product through the FFA; a "free-for-everyone" DDIY product through its website; (3) robust, fully featured DDIY products at low prices; and (4) free electronic filing of state return in the retail channel. As discussed above, the reason TaxACT has been able to play the role of maverick is because, unlike HRB and Intuit, it has less concern about cannibalization.

iii. TaxACT Challenged The Dominance Of HRB And Intuit Through The Free File Alliance

1. TaxACT Disrupted The DDIY Market Thought Its FFA Offer In The First Year

114. In the first year of the FFA,[13] participants offered free federal income tax preparation and e-filing to a fraction of all taxpayers. GX 297 at 87:14-88:5 (Mamo Dep.); Docket #80, IRS Stip. at ¶ 14; GX 29 at ¶ 8 (Intuit Decl.); GX 25 at ¶ 16 (TaxHawk Decl.). Specifically, the majority of companies offered free tax preparation through the FFA to taxpayers with adjusted gross incomes below a certain threshold. GX 31; GX 32. TaxACT, in contrast, was the only firm to offer free tax preparation in the FFA to anyone with an adjusted gross income above $100,000 or who could file using a form 1040EZ. Dunn, TT, 9/7/11 p.m. (Public Tr.), 77:6-13; Dunn, TT, 9/8/11 a.m., 76:5-6; Docket #80, IRS Stip. at ¶ 14; GX 31; GX 32.

115. During the first year of the FFA, TaxACT improved its offer to provide free tax preparation to everyone with an adjusted gross income above $50,000. Dunn, TT, 9/7/11 p.m. (Public Tr.), 77:14-19. When TaxACT changed its offer, other companies followed suit and changed their offers. Dunn, TT, 9/7/11 p.m. (Public Tr.), 78:8-16.

2. TaxACT Disrupted The DDIY Market By Offering All Taxpayers The Ability To Prepare And E-File Their Federal Tax Returns For Free Through The FFA

116. In the second year of the FFA, TaxACT became the first company to offer free federal tax preparation and e-filing for all taxpayers ("free-for-all") through the FFA. GX 28 at 54:11-55:7 (Dunn Dep.); Dunn, TT, 9/7/11 p.m. (Public Tr.), 65:13-25; GX 297 at 136:20-22 (Mamo Dep.); GX 397 at 4; Docket #80, IRS Stip. at ¶ 15; GX 29 at ¶ 8 (Intuit Decl.); GX 25 at

[13] The IRS determined that the most effective and efficient way to decrease the filing burden on taxpayers was to provide greater access to free online tax preparation services. The IRS would work with the FFA, a consortium of companies in the electronic tax preparation and filing industry. Docket #80, IRS Stip. at ¶ 6. Intuit, HRB, and TaxACT were among the original members to offer DDIY products through the FFA. All are current members of the FFA. Docket #80, IRS Stip. at ¶ 8; Bennett, TT, 9/6/11 p.m., 11:2-15; GX 30 at FFA000098.

¶ 16 (TaxHawk Decl.).

117. TaxACT's free-for-all offer through the FFA significantly disrupted the industry. Ernst, TT, 9/7/11 a.m., 23:21-24:2, 26:13-15, 80:8-81:12; GX 1000; Warren-Boulton, TT, 9/8/11 p.m., 22:13-18.

118. TaxACT's free-for-all offer in the FFA caused HRB and Intuit to lose market share and threatened their profitability. GX 35 at HRB-DOJ-00912870; GX 36, GX 29 at ¶¶ 8,11,12 (Intuit Decl.). HRB referred to TaxACT's free-for-all offer as a "land grab," GX 34 at 1, and recognized that "Free for ALL on FFA . . . created a huge disruption in the paid side of the business." GX 39 at HRB-DOJ-50704550; *see also* GX 304 at 3; GX 33 at 2. HRB believed that free-for-all would "ruin the industry," GX 127 at 218:21-219:5 (Bennett Dep.), was a "suicide pact," GX 40, and that HRB's revenues were at risk because free-for-all threatened to cannibalize HRB's software business by causing software buyers to switch to online for free, instead of paying. GX 531 at 114:2-16, 156:9-157:5 (Ciaramitaro Dep.); GX 35.

119. HRB responded to TaxACT by expanding its FFA offer "earlier than planned due to TaxACT 'Free for All.'" GX 304 at 5. Intuit responded to TaxACT by dramatically cutting its DDIY prices as it lost share due to the free-for-all offers on the FFA. GX 1000; Warren-Boulton, TT, 9/8/11 p.m., 22:19-23:17.

120. In response to TaxACT's free-for-all offer, HRB, Intuit and others lobbied the IRS to implement restrictions on the number of customers that could be covered by a free-for-all offer. GX 28 at 114:18-115:9 (Dunn Dep.); GX 28-4; GX 35 at HRB-DOJ-00912870; GX 569 at 108:10-24, 112:1-113:4 (DuMars Dep.); Ernst, TT, 9/7/11 a.m., 26:16-27:4; GX 41 at 4; GX 25 at ¶ 16 (TaxHawk Decl.). HRB expressed its desire to impose restrictions to the IRS and other FFA members because, among other things, it was concerned about how such offers would

affect the pricing structure for the tax preparation industry and remove the ability to generate money through the paid side of its DDIY business. Ernst, TT, 9/7/11 a.m., 26:16-27:4; GX 531 at 60:17-61:9 (Ciaramitaro Dep.); GX 41 at 4; GX 25 at ¶ 16 (TaxHawk Decl.).

121. The FFA rules were amended in October 2005 to prevent FFA members from making free-for-all offers. Dunn, TT, 9/7/11 p.m. (Public Tr.), 78:24-79:9; Ernst, TT, 9/7/11 a.m., 29:3-15; GX 42; GX 25 at ¶ 16 (TaxHawk Decl.); GX 29 at ¶ 9 (Intuit Decl.).

iv. TaxACT Again Aggressively Challenged The Dominance Of HRB And Intuit In The DDIY Market By Becoming The First To Offer Free-For-Everyone Through Its Website

122. In tax year 2005, in response to restrictions that the IRS imposed on the scope of offers that could be made through the FFA, TaxACT became the first DDIY company to offer all tax payers a free DDIY product directly on its website ("free-for-everyone"). Dunn, TT, 9/7/11 p.m., 79:10-80:16; GX 28 at 122:18-123:21 (Dunn Dep.).

123. TaxACT's free-for-everyone offer was maverick conduct that again disrupted the DDIY market.[14] GX 28-7 at 2; Dunn, TT, 9/8/11 a.m., 54:7-19; GX 20 at 9, 11; *see also* GX 35 at HRB-DOJ-00912871. TaxACT described its offer as an "unprecedented offer," GX 43; GX 28 at 131:18-133:1 (Dunn Dep.), and viewed its role in the industry as a "maverick [that] has broken down the barrier for everyone to prepare, print, and now even efile their returns, all for free," GX 3 at 2SS-GRECe-0028583. TaxACT's free-for-everyone "disrupted the then prevalent 'paid' model under which tax preparation software was sold by its competitors." GX 28-9 at 3; GX 28 at 158:14-19 (Dunn Dep.).

124. TaxACT's free-for-everyone offer resulted in increased market share and revenue growth. GX 29 at ¶ 12 (Intuit Decl.); GX 28 at 135:21-136:4 (Dunn Dep.);GX 28-9 at 3.

[14] While other DDIY companies had made free offers in the past, these free offers were substantially limited. For example, Intuit's Tax Freedom Project offer predated the creation of the FFA but the offer had an AGI limitation so it was not free-for-everyone. Ernst, TT, 9/07/11 a.m., 79:2-7; 80:8-81:10.

125. TaxACT's free-for-everyone offer posed a major threat to HRB and Intuit. GX 29 at ¶ 12 (Intuit Decl.); GX 293 at 170:16-17, 181:25-182:9, 185:5-10 (Intuit Dep.). HRB saw an increase in traffic going to TaxACT's website, and TaxACT surpassed HRB in number of online tax preparation clients. Ernst, TT, 9/7/11 a.m., 29:25-30:11; GX 397 at 4. TaxACT's free-for-everyone offer also caused Intuit to lose market share. GX 293 at 163:8-11, 164:20-165:12 (Intuit Dep.).

126. Intuit believed TaxACT's pricing model was "radically unique," GX 29 at ¶ 11 (Intuit Decl.). Intuit became the first DDIY firm to respond to the competitive threat posed by TaxACT's free-for-everyone offer. GX 48 at 6. After testing a free online product in tax year 2006, Intuit the next year offered a free online edition on its home page. GX 48 at 6; GX 29 at ¶ 13 (Intuit Decl.); Dunn, TT, 9/7/11 p.m., 84:21-23; GX 61 at 40:15-41:6 (Houseworth Dep.). According to Ms. Greif, Intuit copied TaxACT's business model after Intuit's CEO told her that TaxACT was "kicking them in the teeth with our marketing strategy." GX 55-6 at 2SS-GRECe-0030506. Intuit subsequently enhanced its free product with an audit support center, a live community, and point of need help in response to TaxACT. GX 293 at 189:16-25 (Intuit Dep.).

127. Meanwhile, HRB held "active discussions" about "how best to compete" with TaxACT's free-for-everyone offer. GX 44. HRB recognized that "Taxact is gaining share both ffa and paid," GX 45 at HRB-DOJ-50098528, and that "some folks are getting nervous that Turbo and TaxAct [are] going to eat our lunch online and we are not going to make our numbers." GX 46. Ultimately, HRB concluded it had to "have a free product to compete in this fast growing segment" which "includes FFA, Free Direct, TaxACT Standard, TurboTax Free Edition, Military One Source, etc." GX 47 at HRB000846.

128. In February 2006, HRB began planning to test "[1040]EZ for free on hrb.com and

taxcut.com," GX 78 at 22, and specifically modified the appearance of its website for these tests in order to better compete with TaxACT. GX 79 at HRB-DOJ-01009830. In tax year 2007, HRB started testing free online. GX 397 at 4. Finally, in 2009, HRB began offering free online products on its website "[t]o match competitor offerings and stem online share loss to Intuit and TaxACT." GX 51 at 4; GX 52 at HRB-DOJ-00250069; Bennett, TT, 9/6/11 p.m., 10:5-11; 44:3-8; GX 127 at 247:13-21, 271:3-11 (Bennett Dep.); GX 397 at 4.

129. TaxACT's launch of its free-for-everyone product had a significant impact on the demand for DDIY products. TaxACT's aggressive marketing of its free product made free tax preparation the expectation of DDIY consumers. GX 61 at 40:15-41:6 (Houseworth Dep.). As Intuit and HRB responded to TaxACT, the share of free online grew. Warren-Boulton, TT, 9/08/11 P.M., 23:18-25:19; GX 20 at 11; GX-127-8; GX 127-12 at 3; GX 144 at 8; GX 1000.

v. TaxACT Continues To Play The Role Of Industry Maverick By Aggressively Competing In The DDIY Market With Its Low Price And Robust Product Offerings

130. TaxACT's consistently low prices, product offerings, and innovative business strategy are another example of its maverick behavior. GX 402; GX 28 at 89:10-14 (Dunn Dep.). TaxACT rapidly gained market share and brand name recognition by offering a full-feature tax preparation product free for use online or as free downloadable software, and at prices that are considerably below its primary competitors. Dunn, TT, 9/7/11 p.m., 97:14-98:9.

131. TaxACT has continually differentiated its products by offering support for more tax forms and schedules than other DDIY products. Dunn, TT, 9/7/11 p.m., 87:6-16. Since 2010, TaxACT's free federal product has supported all federal e-fileable forms, which means that TaxACT's product is "free for everyone." Dunn, TT, 9/7/11 p.m., 87:17-24; GX 55 at 83:5-84:20, 283:1-21 (Greif Dep.). HRB cannot make the same claim because its product does not

support all forms. Dunn, TT, 9/7/11 p.m., 87:25-88:2; GX 55 at 164:7-19 (Greif Dep.). Neither does Intuit. GX 29 at ¶ 4 (Intuit Decl.). Neither do TaxHawk and TaxSlayer. Kimber, TT, 9/12/11 a.m., 43:15-22; Rhodes, TT, 9/12/11 a.m., 99:10-13.

132. Mr. Bennett acknowledged TaxACT's status as an innovator in the market and its strategy to compete with a high quality, lower priced product that "overdeliver[ed] for its customers." Bennett, TT, 9/06/11, P.M., 29:25-30:3; 31: 6-20; *see also* GX 28 at 53:11 (Dunn Dep.). TaxACT's offer of a high quality product at extremely low prices for a long period of time has had a high impact on the DDIY market. Bennett, 9/06/11, TT, p.m., 31:21-32:1; *see also* GX 28-10 at 18; GX 61 at 42:2-3 (Houseworth Dep.); GX 607 at 65:23-66:3 (Liberty Tax).

vi. The Introduction Of Its Product At Staples Is Further Evidence Of TaxACT's Maverick Behavior In The DDIY Market

133. Before November 2010, Intuit and HRB were the only firms selling DDIY products in Staples retail stores. Dunn, TT, 9/7/11 P.M., 118:6-11. In November 2010, pursuant to a licensing agreement with Avanquest, a boxed software version of TaxACT was offered for sale at Staples. Dunn, TT, 9/7/11 p.m., 117:1-118:5; GX 28 at 383:18-384:4 (Dunn Dep.). According to the partnership proposal between TaxACT and Avanquest, [redacted] GX 63 at 1.

134. TaxACT sought to displace HRB as the number two product line at Staples by offering free state e-filing, unlike the retail products of HRB and Intuit, which charge customers an additional fee for state e-filing. GX 293 at 227:2-7 (Intuit Dep.); GX 294 at 135:7-136:9 (Simone Dep.); GX 64, at 2SS-GREC-0001404; GX 61 at 270:17-271:8 (Houseworth Dep.).[15]

135. HRB executives worried that TaxACT's free state e-filing in particular was a

[15] TaxACT also offered a lower price than TurboTax and HRB and free phone support, unlike TurboTax and HRB which both charged $29.99. GX 294-13; GX 294 at 201:5-9; 202:18-22 (Simone Dep.) (Deposition transcript clarifies illegible text on GX 294-13).

competitive threat, GX 294 at 268:10-16 (Simone Dep.), remarking that TaxACT [redacted] GX 61-19. HRB recognized that its retail volume at Staples was "at risk." GX 65 at 2. HRB's concerns were well taken. [redacted] GX 608 (response to question 5).

136. The threat to HRB will likely increase this tax year [redacted] Dunn, TT, 9/8/11 p.m, (Public Tr.), 4:1-3; GX 603; GX 231; DX0334 ([redacted]). Avanquest cited allegations in the Plaintiffs' complaint in this action to show how TaxACT's maverick behavior has benefitted consumers and forced HRB and other competitors to improve their DDIY products and lower their prices. GX 231 at 14-16; DX0334 at 14-16.

137. HRB was forced to respond to TaxACT's entry into the retail channel. [redacted]

138. Intuit was also concerned about the adverse impact that TaxACT's free state e-file offer at Staples would have on the TurboTax strategy of charging for state e-files. GX 293 at 227:8-17 (Intuit Dep.); GX 293-10 at 2. [redacted]

[redacted]

vii. HRB Has Identified The Elimination Of TaxACT's Maverick Conduct As A Benefit Of The Acquisition

139. In 2009, when HRB consider acquiring TaxACT, it was suggested to HRB executives that the merger was a way to "Acquire TaxAct and eliminate the brand to regain control of industry pricing and avoid further price erosion." GX 16 at 20; GX 17 at 3. This remains the rationale for the merger. The analysis of Diamond Management & Technology Consultants, in conjunction with HRB, listed "Elimination of competitor" as a rationale for acquiring TaxACT. GX 171 at HRB-DOJ-00347265. In March of 2010, Mr. Houseworth emailed executives at HRB, "highly recommend[ing]" that they review the Diamond background presentations, as they "provide a great context of the Digital market and opportunity for Block." GX 296-9; GX 296 at 106:8-108:8 (Houseworth Dep.). He also specifically noted that the Diamond presentation discussing "elimination of competitor" contains "a fairly comprehensive overview of the potential models for Digital within the H&R Block business." *Id.*

D. The Acquisition Is Likely To Facilitate Actual Or Tacit Coordination Between HRB And Intuit

140. In addition to elimination of TaxACT as a maverick, structural changes in the market will make coordination more likely. Going from a Big 3 to a Big 2 will make coordination easier. Warren-Boulton, TT, 9/9/11 p.m., 12:20-13:13. This is especially likely here, where "TaxACT has consistently forced the tax preparation industry to become more competitive, and in doing so [has] forced [its] competitors to change as well." GX 28-10 at 18. TaxACT's disruptive conduct has forced its rivals to reduce prices and provide better deals to consumers. Warren-Boulton, TT, 9/08/11 p.m., 25:14-16, 23:4-8. With this restraint removed, HRB and Intuit may recognize that it is not in their mutual benefit to aggressively compete.

Warren-Boulton, TT, 9/9/11, 14:24-15:9.

141. Again, while the United States does not have to prove the precise mechanisms by which HRB and Intuit may coordinate, HRB and Intuit may find it in their mutual interest to reduce the quality of their free offerings. Warren-Boulton, TT, 9/09/11 p.m., 18:16-19:11. The proposed merger increases the likelihood that HRB and Intuit could reach a common understanding about the best way to structure their product lineups to better "up-sell" customers. GX 1006 (Dr. Warren-Boulton Decl.), at ¶ 18. This is true because HRB and Intuit will mutually recognize that free is quite expensive and that the firms would be better off providing free products of lower quality. HRB and Intuit have an economic incentive to offer a lower quality free product and maintain higher prices for paid products because that is "where the money is." Warren-Boulton, TT, 9/08/11 p.m. 33:8-15. As a result, consumers will likely face higher prices or a lower value proposition at the lower end. Warren-Boulton, TT, 9/09/11 p.m., 18:16-19:11.

142. Analyses of the merger by HRB and Intuit confirm Dr. Warren-Boulton's concern that neither firm has the incentive to offer a value proposition in free. In writing about possible reasons HRB might want to acquire TaxACT, Mr. Newkirk wrote that the "other possible strategic consideration is that Intuit and HRB together would have 84% of the digital market and we both obviously have great incentive to keep this channel profitable. Other potential TA purchasers could decide to cut their prices even further to see if they could make large market share gains & build short-term profitability by 'winning the race to the bottom.'" GX 18.[16]

143. Similarly, HRB's Brian Schell wrote that a possible reason for acquiring TaxACT is because "there is value in taking control of this 'segment' by not encouraging a race to free, which Intuit would have no interest in doing, and therefore has value to HRB by preventing it

[16] Although Defendants attempted to downplay Mr. Newkirk's significance, he is the principal analyst who has provided support for the transaction and he is responsible for substantial data analyses for the digital business; he clearly has a full understanding of HRB's business.

through the acquisition." GX 18. Mr. Dunn agreed that HRB would not inherit TaxACT's incentive to be aggressive. Dunn, TT, 9/8/11 a.m. (Public Tr.), 110:4-8.

144. Internal HRB communications suggest that HRB has attempted to coordinate with Intuit in the past. Following the publication of a TaxACT press release highlighting its free-for-all offer, an HRB executive (who later became head of digital) proposed telling retailers that it would be preferable if TurboTax did not respond. GX 145.

145. Intuit's analysis of HRB's likely strategy following the TaxACT acquisition concluded that HRB would [redacted] GX 293-13 at INT-DOJ0015942.

146. Contrary to Dr. Meyer's assertions, the DDIY market has transparent pricing and is therefore susceptible to coordination. Coordination between Intuit and HRB would be effective because the firms offer transparent pricing for comparable products with nearly identical tiers of products, containing similar features. GX 606 at 64:18-20 (Thomson Reuters Dep.); GX 606-2 at 7; GX 294 at 115:22-116:2 (Simone Dep.).

147. [redacted] HRB knows that Intuit raises its prices in the second half of every year and announces on its website the date it will be increasing prices. GX 21, at 259:15-21 (Newkirk Dep.).

148. [redacted] This is only possible because pricing is transparent. [redacted]

149. [redacted]

150. Product features are also very visible. GX 61 at 240:2-3 (Houseworth Dep.). It would not be difficult for HRB and Intuit to coordinate as they each sell four basic DDIY products that have similar features. GX 294 at 72:18-73:12 (Simone Dep.).

151. The DDIY market is also structurally vulnerable to coordination. The transparency of pricing means that DDIY firms can easily collect and verify pricing information, *see generally* GX 615; GX 606 at 64:18-20 (Thomson Reuters Dep.), DDIY transactions are small and numerous, prices can be changed easily, and HRB and Intuit have the opportunity to communicate regularly. GX 61 at 148:14-149:17 (Houseworth Dep.). There are also high switching costs between DDIY products. *See generally* GX 28-24 at 17. For example, TaxACT successfully retains more than 60% of its new users after one year and more than 80% of the users of its products after three years. *Id.*

VI. FRINGE EXPANSION IS UNLIKELY TO PREVENT THE EXPECTED ANTICOMPETITIVE HARMS OF THE MERGER

152. There is no dispute that *de novo* entry would not be timely, likely or sufficient to defeat a price increase. The issue is whether expansion by the fringe firms will be rapid enough to defeat a price increase. Warren-Boulton, TT, 9/20/11 a.m., 12:7-15. The relevant time frame for antitrust analysis, including *de novo* entry, is about two years. Warren-Boulton, TT, 9/20/11, a.m., 12:7-22; Warren-Boulton, TT, 9/09/11 p.m., 104:3-8. Even HRB's CEO, Mr. Cobb admitted that it "isn't credible" to look beyond three years when examining the market. Cobb, 9/19/11 a.m., TT, 63:16-64:7. In considering whether to launch a new DDIY tax preparation brand, HRB concluded that it would take at least three years to gain a meaningful number of

clients and all the while, HRB would lose money. GX 61 at 181:1-6 (Houseworth Dep.). Mr. Dunn believes it would take "a very long time" to build tax software from scratch. Dunn, TT, 9/8/11 p.m. (Sealed Tr. 2:08 p.m.), 13:12-21. In addition, Microsoft tried and failed to enter the DDIY market in 2000. GX 291 at ¶ 9 (Microsoft Decl.).

A. All Digital Competitors Acknowledge That Brand And Reputation Are A Barrier To Entry And That Building A Well-Know Brand Can Take Years And Significant Expenditures

153. TaxACT's 2009 offering memorandum shows how difficult and time-consuming it is to develop a brand: "With over 11 years of building reliable, robust software solutions, 2SS has created a valuable brand within the online tax preparation market which Management believes would take years of competitive investment to replicate." GX 28-24 at 2SS-CORPe-0002419. Mr. Dunn agreed it took 12 years of hard work for TaxACT to build a trusted brand. Dunn, TT, 9/8/11 a.m., 6:22-7:19. Similarly, TaxACT recognizes that taxpayers will not use a DDIY product unless they have "confidence that sensitive data is being handled with care and that returns are processed in a secure, error-free, and timely manner." GX 125 at 12.

154. Mr. Bennett testified that it takes millions of dollars and a lot of time for a small company to develop a brand. Bennett, TT, 9/6/11 p.m., 30:7-10, 63:1-9.

155. Intuit, TaxSlayer and TaxHawk believe success in the DDIY tax preparation category requires a "well-known brand and a good reputation and that developing a good reputation takes years of consistently good performance . . . ." GX-29 ¶ 27 (Intuit Decl.); Rhodes, TT, 9/12/11 a.m., 102:22-103:2-5; GX 25 (Kimber Decl.) at ¶ 13.

156. In response to questioning from the Court, Dr. Meyer agreed that consumer awareness and confidence in the brand are important issues to consider. Meyer, TT, 9/15/11 a.m. (Sealed Tr.), 25:10- 26:9. Nonetheless, Dr. Meyer did not conduct any independent study to

determine the strength of the brands of the firms she claims could expand and she does not know how much more effort it would take for these brands to raise the brand awareness to level comparable to the Big 3. Meyer, TT, 9/15/11 a.m. (Sealed Tr.), 32:3-10.

B. Marketing Costs And Diminishing Returns On Increased Marketing Spend Are A Substantial Barrier To Building Brand Awareness And Attracting Customers

157. Acquiring customers through marketing is expensive. HRB conservatively estimates its incremental marketing costs to acquire DDIY customers at [redacted] per customer. This includes display and search advertising costs as well as affiliate payments to websites for driving online purchases. GX 652 at 178:17-180:10 (Houseworth Dep.). However, this is a conservative estimate of cost to acquire customers through marketing for two reasons: First, it is an average, and second, based on HRB's experience, incremental cost increases as the customer base grows. GX 652 at 180:8-181:11 (Houseworth Dep.). In addition, incremental cost does not account for broadcast advertising, which is necessary to build the brand. GX 652 at 178:17-182:1 (Houseworth Dep.).

158. High levels of marketing effort and expenditure by the large incumbents create and maintain a barrier to expansion by smaller firms. "Two dominant players in the space that invest heavily in marketing will create a barrier to enter the category. Smaller competitors will need to match our spending increases to enter the category. The marketing costs for a startup to break through in the category would be substantial.…" As a result, "smaller competitors" will have to increase their own spending simply "to maintain share." GX 630 at slide 4; *see also* GX 61-23, at 2. [redacted]

159. The fringe competitors are at a significant competitive disadvantage. The efficacy of any attempt to expand through increased marketing efforts is limited by the much larger

marketing effort of the large incumbents. *See generally* GX 478; GX 61-23 at 12; GX-21-30 at 2; GX 607 at 65:8-16 (Liberty Tax Dep.). "Top three category brands [TurboTax, HRB and TaxACT] accounted for [redacted] of digital spend." GX 21-25 at 32. In tax year 2009, the Big 3 combined to spend $[redacted] million on advertising — TurboTax, $[redacted] million, GX 29 at ¶ 38 (Intuit Decl.), HRB, $[redacted] million, GX 61-22 at 3, and TaxACT, $[redacted] million, GX 138 at 37. This disadvantage impedes the ability of the fringe firms to sufficiently replace competition through rapid expansion, even in the aggregate. GX 1451 at 29.

160. Even TaxACT, with its $[redacted] million advertising budget, was unable to gain share last year, demonstrating the challenge faced by the fringe competitors attempting to expand. In tax season 2010, HRB and TurboTax dramatically increased their spending on promotional activities. GX 28 at 65:7-66:8 (Dunn Dep.). As HRB and TurboTax increased their marketing spend, TaxACT could not "stand toe to toe" and "out-advertise them." Dunn, TT, 9/7/11 p.m., 71:17-24. TaxACT lost market share because it had trouble differentiating its free product message and because one TaxACT ad ran once for TurboTax's 25. Dunn, TT, 9/7/11 p.m., 71:17-72:9, 88:3-14.

161. [redacted] GX 28 at 65:7-66:14 (Dunn Dep.); GX 29-6 at 8-9.

162. Expanding manufacturing capacity is not the relevant barrier to expanding the sales of an existing DDIY product; the primary challenge is selling those units. Warren-Boulton, TT, 9/09/11, p.m., 10:2-24.

163. The fringe competitors recognize that they would have to spend a significant amount of advertising dollars to compete against the Big 3. For example, Liberty Tax believes it would have to spend between [redacted] per year, GX 607-3 at ¶ 7 (Liberty Tax Decl.);

CCH could have to spend [redacted] per year, GX 26 at ¶ 4 (Wolters Kluwer Decl.); GX 573 at 84:8-85:9 (Wolters Kluwer Dep.); and Thomson Reuters would have to spend a minimum of [redacted] per year, GX 606 at 72:21-73:4 (Thomson Reuters Dep.). Firms that charge lower prices for their products face an additional competitive challenge, because lower per unit revenues limit what they can spend to advertise their products. GX 28 at 65:18-22 (Dunn Dep.). Even if one or more fringe firms were willing to undertake additional marketing, there are diminishing returns from increased marketing because additional dollars cannot be spent as efficiently as initial dollars. GX 21-31 at 1-2; GX 21 at 192:17-193:14 (Newkirk Dep.).

164. HRB recognizes that increased marketing expenditures are associated with diminished returns and do not guarantee market share growth. When considering the possibility of introducing a new "fighter brand" DDIY product as an alternative to acquiring TaxACT, [redacted] GX 21-32 at slide 19; GX 223 at HRB-DOJ-00013482. [redacted] GX 21-32 at slide 19. [redacted] *Id.*

165. As a result of the steep diminishing returns associated with increased marketing in

the DDIY market, Mr. Newkirk estimated that, if HRB were to introduce a new brand and were to increase the annual marketing expenditure for the new product from $[redacted] to $[redacted] the incremental $[redacted] and would produce [redacted] clients at a cost of $[redacted] GX 21-31 at 1; *see also* GX 21 at 458:10-459:15 (Newkirk Dep.). Mr. Houseworth similarly concluded that HRB [redacted] $[redacted] to $[redacted]. GX 21-32 at slide 19.

C. Need For Word Of Mouth Referrals Is A Significant Barrier To Rapid And Sufficient Expansion

166. Word of mouth referrals are critical to drive consumer awareness. *See* Dunn, TT, 9/7/11 p.m., 106:10-15; Warren-Boulton, TT, 9/9/11 p.m., 11:11-16; *see also* GX 28-24 at 15. However, the process of building a brand through word-of-mouth referrals is time-consuming. GX 28 at 279:3-280:11 (Dunn Dep.).

167. Nearly [redacted] percent of TaxACT's online customers in tax year 2008 were referred by a friend or relative. GX 28-24 at 16. TaxACT relies on word of mouth advertising to perpetuate its growth because it cannot out-advertise HRB and TurboTax. Dunn, TT, 9/7/11 p.m., 71:17-72:9. Mr. Dunn acknowledged that it took time to build a brand through word of mouth referrals. *Id.* at 106:10-22. Ms. Greif explained that word of mouth advertising reflects customer satisfaction with the DDIY product, and this satisfaction cannot be developed through a marketing investment. GX 55 at 93:20-94:11 (Greif Dep.).

168. As Dr. Warren-Boulton explained, it is very challenging for a small firm to grow through word-of-mouth referrals because its existing customer base is small. Warren-Boulton,

TT, 9/20/11 a.m., 13:16-25; *see* GX 25 at ¶ 13 (TaxHawk Decl.). As a result, Dr. Warren-Boulton does not expect the percentage of growth that is created off of a small base will make a price increase unprofitable because it would take too long and may never happen. Warren-Boulton, TT, 9/20/11 a.m., 13:16-25.

D. Market Conditions Under Which TaxACT Became A Significant Competitor Were Much More Favorable To Expansion Than Current Conditions

169. First, TaxACT has benefitted from a first mover advantage. When TaxACT offered its free-for-all product in the FFA in 2003, none of the other FFA products had an offer as broad as TaxACT's. Dunn, TT, 9/7/11 p.m., 65:21-25. When TaxACT offered its free-for-everyone product from its website in tax year 2005, no other firm imitated TaxACT's offer that year, which gave TaxACT a jumpstart over the competition. *Id.* at 80:11-19.

170. Intuit acknowledged that TaxACT's status as a first mover allowed the firm to attain competitive significance. TaxACT had the advantage of being the first to offer free to prepare and e-file DDIY products from its website, and it remained the only significant firm that satisfied customer demand for those two products for two tax seasons. GX 29 at ¶ 12 (Intuit Decl.). Intuit believed that as a result TaxACT's market share grew. *Id*. This compares to the opportunity presented to small rivals post-merger of an 8 to 10 percent unilateral price increase on the TaxACT product, which is not going to induce a supply response by the other firms large enough to deter the price increase. Warren-Boulton, TT, 9/9/11 p.m., 9:9-11:23.

171. As discussed in Section VI.B above, the increased marketing expenditures and large installed base of the incumbents make it extremely hard for a firm to expand relative to TaxACT nine years ago.

172. Increasing marketing expenditures have driven up the cost to acquire customers. HRB found that its CPA (cost per acquisition) on Yahoo Search [redacted] from $[redacted] in tax

season 2009 (without inclusion of discontinued Yahoo program) to $[redacted] in tax season 2010, GX 21-25 at slide 6, and that the CPA for its online affiliate marketing [redacted] from $[redacted] in FY09 to $[redacted] in FY10, and was forecast [redacted] to $[redacted] in FY11, GX 88 at 45.

173. Similarly, TaxACT's CPA has [redacted] since tax year 2004. The CPA of all customers [redacted] from $[redacted] in tax year 2004 to $[redacted] in tax year 2010, and the CPA of total advertising [redacted] from $[redacted] in tax year 2004 to $[redacted] in tax year 2010. GX 151 at 7. A firm trying to expand its customer base would now encounter CPAs similar to or larger than TaxACT's CPA for outside advertising, which is entirely focused on new customer acquisition. GX 55 at 99:12-18, 114:9-115:2 (Greif Dep.).

174. Third, the DDIY market has matured. Historically, new DDIY customers came from the pool of pen and paper users. Today, however, the pool of pen and paper customers is rapidly shrinking, which limits the ability of expansionary firms to gain new customers. GX 61 at 172:9-173:11, 188:12-189:14 (Houseworth Dep.). As a result, the DDIY market's growth could level off within 3 years. *Id.* 190:1-4.

175. In addition, expansion today is more expensive and difficult because competing in a mature market requires spending additional marketing dollars to steal customers from existing competitors, which is very difficult because many customers are reluctant to switch. GX 21-31 at 2. [redacted] GX 21-28 at HRB-DOJ-50024541.

E. TaxSlayer And TaxHawk Are Unlikely To Expand Sufficiently To Mitigate The Acquisition's Anticompetitive Effects

176. Dr. Warren-Boulton opined that in response to an anticompetitive price increase, neither TaxSlayer nor TaxHawk have the incentive or ability to significantly expand to defeat such a price increase. Warren-Boulton, TT, 9/20/11 a.m., 14:1-16:2. He noted that the market is

characterized by high margins of 70-80%, which already provide TaxSlayer, TaxHawk, and other fringe firms, the incentive to increase sales. *Id.* at 14:24-15:5. Despite these incentives, Intuit estimated the market share of the whole category of "other," which includes TaxSlayer and TaxHawk, has declined from 10% in tax year 2003 to 8.4% in tax year 2009. GX 29-3 at 12. Looking forward, Dr. Warren-Boulton's economic model, that predicts price increases by HRB and TaxACT, takes into account an increase in sales by TaxSlayer and TaxHawk. Warren-Boulton, TT, 9/20/11 a.m., 14:4-15. However, he sees nothing to indicate that TaxSlayer and TaxHawk are going to fundamentally change to become better competitors or increase their incentives to spend on marketing. *Id*. at 14:16-15:15.

177. TaxSlayer and TaxHawk are very differently positioned in the DDIY market now than TaxACT was before its free-for-everyone offer led to its expansion. "TaxACT was in a position where the kind of particular actions it took within the FFA and on the Web site, where it was really able to exploit those openings. And the reason is, is because it already had a pretty significant share." Warren-Boulton, TT, 9/9/11 p.m., 17:10-17:15. TaxHawk and TaxSlayer have about 3% each of the DDIY market, while TaxACT had 8% share before it grew through its free-for-everyone offer. GTX 17; Meyer, TT, 9/15/11 a.m. (Sealed Tr.), 34:9-35:15. Moreover, TaxHawk and TaxSlayer had a combined growth rate of [redacted] in the DDIY market over the past five years. GTX 17; Meyer, TT, 9/15/11 a.m. (Sealed Tr.), 33:5-11, 35:11-15.

178. Thus, it is not surprising that HRB [redacted]. *See generally* GX 61 at 61:21-62:4 (Houseworth Dep.) ([redacted].

i. TaxSlayer

179. TaxSlayer's market share, based on federal e-files, [redacted]

[redacted] TaxSlayer expressly attributes its failure to gain share to its inability to keep up with the advertising spend of HRB, Intuit, and TaxACT. GX 113 at ¶ 14 (TaxSlayer Decl.).

180. TaxSlayer is no maverick. TaxSlayer urged that offer restrictions be implemented in the FFA following the 2004 tax season. GX 28 at 115:18-21 (Dunn Dep.). Its free product is only offered to Form 1040EZ filers and active duty military. Dunn, TT, 9/8/2011 a.m. (Public Tr.), 66:4-9. TaxSlayer is also not big enough to replace TaxACT as a maverick. Warren-Boulton, TT, 9/09/11 p.m., 17:10-18:04.

181. TaxSlayer does not currently have a product comparable to the products offered by the Big 3. Unlike the Big 3, TaxSlayer does not have: (1) either a downloadable product for new customers or CD version of its software for sale through retailers; (2) functionality for consumers to import data such as W-2s and 1099's into their tax returns; or (3) the ability to import a prior year's tax return from another digital tax preparation provider. Rhodes, TT, 9/12/11 a.m., 99:17-100:18.

182. TaxSlayer expects to spend [redacted] on marketing/advertising in tax year 2011, GX 113 at ¶ 12 (TaxSlayer Decl.), and has [redacted] TaxSlayer does not know of any way in which it could double its size in one to two years. Rhodes, TT, 9/12/11 a.m., 103:10-12. "[T]here is no silver bullet for a small company to grow market share quickly." *Id.* at 103:13-15.

ii. TaxHawk

183. TaxHawk cannot replace TaxACT as a maverick. Warren-Boulton, TT, 9/20/11 a.m., 14:4-15:8. [redacted]

184. TaxHawk has experienced modest growth since launching its DDIY products in 2002. *See* Kimber, TT, 9/12/11 a.m. (Public Tr.), 11:5-12. In tax year 2010, TaxHawk prepared approximately [redacted] federal tax returns and earned $[redacted] in revenues. Kimber, TT, 9/12/11 a.m. (Sealed Tr.), 62:19-21, 67: 9-10. And from tax season 2006 to tax season 2010, TaxHawk has only grown its DDIY market share from [redacted] to [redacted] *Id.* at 64:13-16.

185. Unlike the Big 3, TaxHawk does not: (1) support all federal forms and schedules; (2) the states of Tennessee and New Hampshire; and (3) many forms for the states it does cover, including non-year resident and part-year resident forms; and (4) forms for cities that have income tax requirement such as New York and Detroit. Kimber, TT, 9/12/11 a.m. (Public Tr.) 13:3-9; 43:15-45:4. Thus, there are at least 26 million people for whom TaxHawk is not a viable option. It will take TaxHawk two to three years to develop state non-year resident and part-year resident forms and ten years to develop forms for cities with tax filing requirements. *Id*. at 44:8-17, 45:9-18. It would also require a change in the company's "lifestyle" culture, which it is unwilling to make. *Id.* at 45:15-19. Also, unlike the Big 3, TaxHawk does not offer: (1) downloadable and box products; (2) refund anticipation checks; (3) functionality to import data from competitors' products; (4) phone support; or (5) functionality to import W-2 and 1099 data.

Id. at 42:13-43:2, 45:20-48:9.

186. Even if TaxHawk were to develop such a product, [redacted]. While TaxHawk could increase its customer base by significantly increasing its marketing expenditures, "TaxHawk is comfortable with the same gradual growth of [its] customer base that it has experienced over the past several years." GX 25 at ¶ 14 (TaxHawk Decl.). [redacted]

F. No Other Fringe Competitor Is Likely To Replace In A Timely Manner The Competitive Rigor Now Exercised By TaxACT

187. <u>OnePrice Taxes</u>: OnePrice Taxes processed approximately [redacted] returns for tax year 2010 and spends approximately [redacted] annually on marketing. GX 654 at 8:18-20 (OnePrice Taxes Dep.); GX 155 at ¶ 3 (One Price Taxes Decl.).

188. OnePrice Taxes' goal is to process [redacted] consumer tax returns annually within five to ten years. GX 155 at ¶ 3(OnePrice Taxes Decl.) [redacted]

189. <u>On-Line Taxes</u>: Consumers used On-Line Taxes to process between [redacted] and [redacted] tax returns for the 2010 year. GX 570 at 6:8-13 (On-Line Taxes Dep.). On-Line Taxes' DDIY product generated approximately $[redacted] in revenues for fiscal year 2010. *Id.* at 58:7-12. On-Line Taxes has a [redacted]

190. [redacted]

[redacted]

191. Wolters Kluwer (CCH): In tax year 2010, CCH's "Complete Tax" DDIY product processed [redacted] tax returns, generated revenues of $[redacted] and incurred expenses of approximately $[redacted] GX 573 at 101:4-15, 118:23-119:11 (CCH Dep.). CCH's Complete Tax engine also provides a platform for about one dozen partner affiliates who market the product under their own brands, including Liberty and Jackson Hewitt. *Id*. at 68: 2- 70:17. In tax year 2010, these partner affiliates collectively processed [redacted] returns. *Id*. at 119:3-11.

192. [redacted]

193. JTH (Liberty): Liberty believes TaxACT's acquisition by HRB will make expansion more difficult. GX 607-3 at ¶ 8 (Liberty Decl.). Currently, Liberty licenses its DDIY product from CCH. [redacted]

194. In the most recent tax year, Liberty's eSmartTax handled only 106,000 tax returns. *Id*. at 12:4-5. Liberty Tax hopes to have [redacted] DDIY customers by 2016. *Id*. 59:10-13. [redacted]

[redacted]

195. Petz Enterprises: After eleven years in the DDIY industry, Petz Enterprises "Taxbrain" DDIY product is only used to process approximately [redacted] individual tax returns each year, translating into a [redacted] market share. GX 571 at 83:11-84:14 (Petz Dep.). [redacted]

196. Thomson Reuters: In tax year 2010, Thomson Reuters' TaxSimple DDIY product was used to prepare approximately [redacted] tax returns and earned approximately [redacted] GX-156 at ¶ 5 (Thomson Reuters Decl.).

197. [redacted]

198. [redacted]

VII. DEFENDANTS' PURPORTED EFFICIENCIES DO NOT SAVE THIS TRANSACTION

199. Plaintiff's financial accounting expert, Dr. Mark Zmijewski, examined the Defendants' efficiency claims in light of principles from the Horizontal Merger Guidelines requiring that such claims be (a) verifiable, and (b) merger specific, in that they could not be achieved on a stand-alone basis. Zmijewski, TT, 9/19/11 a.m. (Public Tr.), 96:1-20, 97:12-16. For verifiability, Dr. Zmijewski analyzed the Defendants' calculations to determine the factual

basis for each input – whether a fact or an assumption – and to determine whether the Defendants' calculations were reliable and reproducible using standard accounting methods. *Id.* at 100:1-18, 101:2-21. For merger-specificity, Dr. Zmijewski considered whether the companies' calculations accounted for cost savings that the firms could achieve on a stand-alone basis, since such savings are not cognizable, merger-specific efficiencies. *Id.* at 97:12-16, 97:23-98:3.

200. Dr. Zmijewski found that, of the Defendants' eleven efficiency claims, only one was verifiable. *Id.* at 101:25-102:2. In general, the Defendants' calculations failed to account for efficiencies that they could achieve on a stand-alone basis. That is, the calculations did not reduce current costs to the cost that HRB would spend if it achieved the efficiencies on its own. *Id.* at 102:5-9. Further, TaxACT's cost assumptions were a key input to the efficiency calculations, but those assumptions could not be verified because they were not based on, nor checked against, previous changes in volume and historical incremental costs. *Id.* at 102:10-24. The significant problems with Defendants' calculations are discussed in succeeding sections below.

A. Defendants' Claimed Efficiencies Must Be Considered In Light Of HRB's Past Failed Attempts To Obtain Efficiencies From Acquisitions

201. HRB has a history of failing to achieve efficiencies from acquisitions. Bennett, TT, 9/6/11 p.m. (Public Tr.), 64:11-18. In fact, according to Mr. Newkirk, HRB has never become more efficient after an acquisition. Newkirk, TT, 9/7/11 a.m. (Public Tr.), 95:3-11. HRB's past history does not support its claimed ability to achieve efficiencies here. GX 664 at ¶¶ 19-20 (Zmijewski Report).

202. For example, HRB previously acquired a software company called TaxWorks, renamed "RedGear," with the hope that [redacted]

[redacted]

203. For the RedGear acquisition, HRB had only projected a total of $[redacted] million in synergies over 3 years but failed to achieve them. GX 459 at 5. HRB's synergy projections for this transaction are much more aggressive in that it estimates it will achieve $[redacted] million run-rate synergies, annually, through at least Fiscal 2017. Bowen, TT, 9/15/11 p.m. (Sealed Tr.), 89:24-90:4, 90:10-16.

B. The Purported Efficiencies From The Transaction Are Predominantly Not Merger-Specific

204. Even if they were realistic in light of Defendants' past history of failing to obtain efficiencies, the claimed efficiencies are not merger specific. Defendants' senior managers believe that HRB can improve its efficiency on its own:

205. Generally, HRB's CEO who negotiated the deal, Mr. Bennett, believed HRB could cut costs on its own as a means of competing for share, along with improving its product and its marketing. Bennett, TT, 9/6/11 (Pubic Tr.) a.m., 103:2-14. Mr. Bennett also believed HRB could achieve projected Year One efficiencies without acquiring TaxACT. Bennett, TT, 9/6/11 p.m., 63:22-64:10.

206. Mr. Dunn also believes that the transaction is not necessary to achieve the claimed efficiencies. According to Mr. Dunn, if he were hired to manage HRB's business in the absence of a merger, he could get HRB's cost to "emulate 2nd Story's cost." Dunn, TT, 9/8/11 p.m. (Sealed Tr.), 7:10-15. While Mr. Dunn states it would take longer than [redacted] to get HRB's standalone costs to "emulate 2nd Story's cost," HRB's own projected synergies from the transaction itself are not fully achieved until [redacted]. DX 236 at DX 0236-007; Zmijewski, TT, 9/19/11 p.m. (Sealed Tr.), 15:24-16:16.

207. More specifically, Defendants claimed that they could reduce the IT costs for the development and production of online and hard copy software products by more than [redacted] percent. Zmijewski, TT, 9/19/11 a.m. (Sealed Tr.), 118:13-25. These savings represent nearly [redacted] percent of the total projected synergies by year three. *See* DX 236-07. To support this claim, Defendants offered the testimony of Mr. Bowen, who said that much of this savings would come from combining two existing HRB software platforms into a single TaxACT platform. But Mr. Bowen's testimony was not persuasive; he admitted that he did not understand the underlying technology, was not the person assigned to determine the IT synergies, and could not opine on whether HRB could combine its IT platforms on its own. Bowen, TT, 9/19/11 a.m., 12:16-21, 9/19/11 p.m., 24:15-17. He deferred to HRB's CIO, Mr. Agar, who was not called as a witness by HRB. Zmijewski, TT, 9/19/11 a.m. (Sealed Tr.), 110:15-111:6. Mr. Agar's absence is not surprising since he testified at his deposition that HRB could combine its online and software platforms in a single platform without incurring any incremental expenses and it would result in saving approximately [redacted] percent of the [redacted] HRB spends annually on its software product. GX 605 at 36:6-15, 39:5-45:17, 48:19-49:4 (Agar Dep.).

208. Mr. Agar is confident that he has the right managers in place to evaluate HRB's ability to complete the project. *See* Bowen, TT, 9/19/11 a.m. (Public Tr.), 17:7-12. In 2010, HRB "put on the shelf" the possibility of consolidating its online and software platforms because of the potential acquisition of TaxACT. GX 605 at 33:18-34:4 (Agar Dep.).

209. With respect to other efficiencies, HRB has recently studied bringing the [redacted] of its [redacted] in-house. GX 664 at 41-42 (Zmijewski Report). However, the results of the study were not produced. *Id*. Similarly, HRB has studied bringing its [redacted] in-house, but opted not to do so. GX-530 at 208:11-209:6 (Bowen Dep.). Bowen did not know the

details of that decision, and Defendants have not produced the results of this analysis. GX-664 at 123 (Zmijewski Report). The defendants have thus not demonstrated the merger-specificity of these efficiencies.

210. Likewise, some proportion of projected call-center savings, and possibly all of them, could be achieved without purchasing TaxACT. Zmijewski, 9/19/11 p.m. (Public Tr.), 4:9-14. HRB attributes its [redacted] efficiency to location-based labor costs, higher [redacted] due to product "glitches," and TaxACT's "cost-conscious culture." GX-131 at 152:18-153:7, 160:20-161:21 (Bowen Dep.). But HRB acknowledges that it could move its [redacted] to obtain lower labor costs, and further states that it has been able to greatly reduce product "glitches" on its own. *Id*. at 166:11-15; GX 61 at 31:12-15 (Houseworth Dep.). If it chose, HRB could utilize "best practices" similar to those that TaxACT has identified, such as having the developers of state forms respond to user questions about those forms. Bennett, TT, 9/6/11 p.m., 76:4-20.

211. Regarding its [redacted], HRB claims that TaxACT will save costs by hiring new individuals and bringing their functions in-house, but HRB apparently failed to consider the possibility of taking this step on its own. GX 21, vol. 2 at 615:5-9 (Newkirk Dep.); Zmijewski, TT, 9/19/11 p.m. (Sealed Tr.), 48:13-24. Such in-sourcing is a standard way to save mark-ups and overhead, and one can predict that HRB would take this step in order to save money, if the transaction does not go through. Zmijewski, TT, 9/19/11 p.m. (Sealed Tr.), 49:4-10.

C. TaxACT's Post-Merger Cost Estimates Are Not Verifiable

212. Even if merger-specific, the claimed efficiencies are not verifiable. The main cost efficiencies were calculated by taking HRB's current cost, and comparing them to a measure of

TaxACT's incremental cost to do the same activity. Bowen, TT, 9/19/11 a.m. (Public Tr.), 10:9-16. Thus, the TaxACT cost estimates were an important input to the calculation. *Id*. at 10:17-21.

213. However, TaxACT's cost estimates were "not the results of facts and objective verifiable analyses using appropriate methodologies. As such, the TaxACT incremental cost estimates cannot be verified." GX 664 at 25.

214. For example, to arrive at the human resources required to accomplish the integration tasks, TaxACT did not use any mathematical calculation or analysis, and based its assessment purely on the judgment of the four founders and the management team. GX 657 at 30:11-19 (Dunn Dep.). Similarly, no mathematical analysis or calculations were done to determine the purported efficiencies relating to hardware costs. *Id.* at 37:10-11.

215. Though Mr. Dunn claimed at trial that the determination of the efficiencies took "hundreds of hours," 9/8/11 p.m. (Sealed Tr.) at 39:24, Ms. Greif participated in the TaxACT cost estimate process and described it as follows: "[a] round table discussion amongst the four or five of us and roughly how many people we thought we would have to add, roughly how many servers we might have to look at acquiring, those types of things." GX 55 at 329:11-15 (Grief Dep.). The resulting spreadsheet had "some numbers thrown together," and the process was not "long" or "drawn out," but was "something that we kind of back of the envelope put together." *Id*. at 332:10-13.

216. Ms. Greif's description of the process is more credible than Mr. Dunn's. The Preliminary Integration Cost Analysis that TaxACT sent to HRB was indeed a spreadsheet. The original version of the sheet that TaxACT sent to HRB in August 2010 is similar in structure and content to the version that HRB used for its efficiencies claims at trial. *Compare* GX-131-9 at 5 to DX-236 at 8. The only changes to contents of the "HR Description" column presented at trial

are certain increased resources to the [redacted] and a decrease of [redacted] the other values for the HR Description column are unchanged between the versions. *Compare* GX-131-9 at 5 (the August 2010 version) to DX-236 at 8 (the trial version).

217. As part of its cost projections, TaxACT did not conduct, or at any rate did not disclose, any analysis of TaxACT's past changes in volume of activity and its incremental cost as a result of such changes. Zmijewski, TT, 9/19/11 a.m. (Sealed Tr.), 118:9-12.

218. TaxACT's cross-checking of its integration cost projection consisted solely of a "reality check" that involved "opening the financial statements" and "compar[ing] it with what we're costing here." GX 657 at 32:22-33:1; 33:23-34 (Dunn Dep.)

219. Mr. Dunn checked TaxACT's "trial balance," but this is a static cost report. *Id*. at 33:23-34:1 (Dunn Dep.); Zmijewski, TT, 9/19/11 p.m. (Sealed Tr.), 20:12-18. Mr. Dunn did not check the cost projections against past incremental changes in cost or headcount at TaxACT that resulted from prior changes in scope of activity. Zmijewski, TT, 9/19/11 p.m. (Sealed Tr.), 20:8-12, 19-23. Thus his analysis did not address the question of incremental costs, *i.e.*, whether TaxACT has become more efficient, less efficient, or otherwise, as its size has changed. Zmijewski, TT, 9/19/11 p.m. (Sealed Tr.), 26:13-23; 38:4-8. This is a standard part of a cost analysis. *Id.*

220. The four TaxACT founders recorded their task list for the integration project on a white board. Dunn, TT, 9/8/11 p.m. (Sealed Tr.), 20:8-9, 21:1-4. However, the contents of the white board were not written down nor disclosed via interrogatory or otherwise. Zmijewski, TT, 9/19/11 (Sealed Tr.), 18:19-19:6. There was a lot more on the white board that was not documented to HRB. Dunn, TT, 9/8/11 p.m. (Sealed Tr.), 21:14-21. The document provided to

HRB (and produced in discovery) was "summarized" to exclude implementation strategies that TaxACT considered proprietary. *Id.* at 21:16-19

D. HRB Has Not Demonstrated Why Its "Management Culture" Cannot Be Improved Without Acquiring A Competitor

221. TaxACT's superior efficiency versus HRB today is due to its "cost culture" and its possession of more "seasoned" and "capable" management than HRB. Bennett, TT, 9/06/11, P.M., 74:11, 76:4-9, 21-24, 108:20-22; 70:6-11; Bowen, TT, 9/16/11 p.m. (Sealed Tr.), 107:23-108:3; GX-131 at 56:9-11 (Bowne Dep.). TaxACT's superior culture includes: (1) its preference for in-sourcing versus out-sourcing, GX-131 at 168:18-20 (Bowen Dep.); (2) its avoidance of "large firm" behaviors which tend to be less efficient, *Id.* at 63:3-15; (3) its "consistent" strategy as distinct from the "different pricing and market share strategies" that HRB has had "every year for years," Bennett, TT, 9/6/11 p.m., 48:17-19,70:9-11, 72:3-7; and (4) its use of efficient processes such as having the person who develops a tax form, answer users' questions about that form during tax season. *Id.* at 76:4-20.

222. Senior managers at HRB have proposed changes to the digital organization, short of merger, to achieve results closer to what HRB hopes to gain from utilizing TaxACT's "seasoned" management. Absent this transaction, HRB's Board Chairman had proposed that HRB "commit resources to build mass" for digital, and "recruit someone capable of building it," a manager of "Bill Cobb's stature, but running digital every day." GX-611 at 1.

223. [redacted] GX 101 at 2.

224. Under its previous management, HRB's digital business had a "revolving door"

and went "guardrail to guardrail" in terms of strategy. GX-61, 24:8-18 (Houseworth Dep.); Bennett, TT, 9/6/11 p.m., 48:17-19; 72:3-7. HRB could choose to implement a more consistent strategy for its Digital business if it wished, and could expect to achieve benefits similar to those that TaxACT enjoys from its consistent management and strategy.

225. Mr. Bowen acknowledges that Fortune 500 companies regularly announce efforts to change their cultures to one of cost control, and any company can attempt to change its culture. Bowen, TT, 9/15/11 p.m. (Sealed Tr.), 108:6-11.

226. Even Dr. Meyer concedes that this merger is not necessary to change HRB's "cost culture." Meyer, TT, 9/15/11 a.m. (Sealed Tr.), 15:4-19. TaxACT's efficient processes are not claimed to be trade secret or proprietary. *See* GX 55-7 at 42-47 (Zmijewski Dep.).

E. Defendants' "Emerald Card Efficiency" Is Incorrectly Calculated

227. The Emerald Card claim measures higher revenue post-transaction, which is not a cognizable cost efficiency under the Merger Guidelines. Zmijewski, TT, 9/19/11 p.m. (Sealed Tr.), 10:12-25.

228. Defendants' documents describe the Emerald Card claim as a "revenue synergy." DX 236-010 (citing "Revenue Synergy" of $[redacted]M). The Emerald Card efficiency itself will result from TaxACT getting the "whole piece of the pie" in terms of bank fee revenue associated with the cards, rather than having to share revenues with a third-party bank. Dunn, TT, 9/8/11 p.m. (Sealed Tr.), 7:4-7. Post-merger, TaxACT would no longer have to share those fees with a third party. GX 131, 188:10-14 (Bowen Dep.).

229. Defendants' method of calculating the synergy compares post-merger earnings, so it includes both revenue and expenses. Zmijewski, TT, 9/19/11 p.m. (Sealed Tr.), 5:12-19. Thus, the calculation includes revenue synergies that are not part of cognizable efficiencies. *Id.*

230. [redacted]

F. Pass Through Of Merger-Specific Savings Is Unlikely

i. Most Projected Savings Are Fixed Cost Savings Which Do Not Improve Consumer Welfare

231. In any event, Defendants acknowledge that over [redacted] of their claimed efficiencies represent anticipated savings of fixed cost, not variable cost. DX-17 at 39, Table 4 (Meyer Report), (citing [redacted] in fixed cost efficiencies vs. $[redacted] variable).

232. For merger analysis, where the concern is the effect on consumer welfare, cost improvements from efficiencies should only be taken into account when they reduce variable costs. Cost improvements in fixed costs may make the parties better off but do not change their incentives as to what price to choose. Warren-Boulton, TT, 9/9/11 p.m., 4:20-5:05; 7:12-7:25.

233. Dr. Meyer contends that fixed-cost savings could have pro-competitive effects by giving HRB increased "flexibility" to engage in increase advertising spending or to lower prices. DX0017 at 92 (Meyer Report). However, Dr. Meyer does not explain why, given that HRB already earned profits of $[redacted] and $[redacted] in FY10 and FY11, it could not have already increased its advertising or reduce its prices. DX-9022.

234. Overall, HRB projects that its efficiencies will go to shareholders in the form of higher profits, not to consumers as lower prices. When HRB's Board voted to approve the transaction, the financial model that they utilized, originating at Greenhill and incorporated into the Board's materials by Mr. Bowen, showed the projected synergies going not to consumers, but to shareholders in the form of increased profits, dollar-for-dollar. GTX 1465 at 1930;

Bowen, TT, 9/19/11 a.m. (Sealed Tr.), 24:12-25:1; 25:6-13.

235. Although operationally, HRB plans to move users to TaxACT's less-costly platform, [redacted]. GX 530 at 300:12-30 (Bowen Dep.) Rather, HRB plans to continue charging premium prices. Bennett, TT, 9/6/11 a.m., 102:2-14.