The Contribution of Merger Control to the Definition of Harm to Competition

Carles Esteva Mosso

Introduction

As you know, in September last year, we celebrated the 25th anniversary of the entry into force of the EU Merger Regulation – Council Regulation 4064/89.

This event prompted interesting debates on the historical evolution of EU merger control. We may have not examined in detail, however, a very specific feature of these 25 years: the mutual interaction between an emerging merger control regime and a well-established system of enforcement of Articles 101 and 102 TFEU. I am very grateful to the GCLF, as always at the forefront of antitrust thinking, for providing me today with this opportunity to share some thoughts on this matter.

I will first outline how EU merger control has been influenced by its "older cousin", antitrust enforcement, and how, in particular after the reform of 2004, it converged towards antitrust standards. I will then examine the significant contribution merger control has conversely given to antitrust. On this basis, I will, in the conclusion examine whether there exists (or should exist) a single analytical framework for the analysis of agreements and horizontal mergers, under Article 101 and the Merger Regulation respectively.

The convergence of merger control towards antitrust

EU merger control is « the child » of both Articles 101 and 102 TFEU – as you know, it was through the application of then Articles 85 (Philip Morris) and 86 of the Treaty (Continental Can) that the Commission and the Court of Justice first proceeded to control concentrations in the EU. However, when the Merger Regulation was enacted the legislator considered that the "creation or strengthening a dominant position", a concept emanating from Article 86, constituted a better foundation for the substantive assessment in merger control.

As a result, in the early years, the assessment of mergers was conceptually very different than the assessment under Article 101 of other types of agreements between undertakings, less structural in nature than mergers.

Not only the substantive tests diverged: the "creation or strengthening of a dominant position" was quite far apart from that of an agreement or practice "having the object or effect of restricting competition". Also the interpretation of both tests contributed further to the divergence of standards. In particular, under the previous, more form-based approach to the interpretation of “restriction of competition”, a large number of agreements were considered to be caught by the test of Article 101(1) and required exemption under Article 101(3), either by formal decision (rarely) or by comfort letter (more common). On the other hand, the dominance test in mergers was applied on the basis of the jurisprudence developed under Article 102 and found to be met in only a small proportion of the large number of mergers scrutinized by the Commission every year. Once dominance was found, no efficiency defence was considered to be available.

This divergence of standards, which in practice lead to a more lenient treatment of horizontal mergers than to collusive agreements between firms holding similar amounts of market power (also referred to as “concentration privilege” “Konzentrationsprivileg” in German), seems, with hindsight, difficult to explain. Why, let's say, a joint distribution agreement between companies holding a 30% market share could be caught by Article 101 while a merger between the same companies could be cleared unconditionally? This divergence of treatment could only be premised on an implicit presumption of efficiencies in mergers, which would justify the clearance of operations below the level of dominance. Such a general presumption, however, appears today as a very theoretical construct, difficult to support empirically.

The reform of EU merger control in 2004 changed this situation. By attempting to move away from an excessively structuralist analysis in merger control towards a more effects based one and to close a gap with respect to cases leading to unilateral effects in a non-collusive oligopoly, it actually brought the substantive analysis under merger control and Article 101 much closer than in the past.

First, the new test of “significant impediment to effective competition” or SIEC introduced in merger control a standard conceptually more similar to the « restriction of competition » under Article 101. The SIEC test does not require the finding of dominance but a lower level of market power and focuses on the likely impact of the merger in the main market competition parameters (price, output, innovation,…).

Further, the recast Merger Regulation brought the structure of the merger assessment closer to the one of Article 101 TFEU. It now explicitly recognizes in Recital 29 (and the Commission’s Horizontal Merger Guidelines provide further guidance) that efficiencies brought about by a merger may counteract its possible anti-competitive effects and thus not lead to a SIEC – in a very similar way to an agreement or practice meeting the test of Article 101(1) TFEU but not infringing that prohibition if the conditions of Article 101(3) are met. In both instances,

- the restriction of competition according to Article 101(1) must be necessary to obtain them, or respectively, the efficiencies must be "merger-specific";

- the restriction of competition must allow "consumers a fair share of the resulting benefit", or respectively, the efficiencies resulting from the merger must be "passed on to consumers";

- finally, while under Article 101(3) a restriction of competition may not afford the parties "the possibility of eliminating competition in respect of a substantial part of the products in question", the Horizontal Merger Guidelines state that a merger resulting in a near-monopoly is unlikely to produce efficiencies large enough to exclude a SIEC.

And both under Article 101(3) TFEU and the efficiency defence under the Merger Regulation, the burden of proof that the efficiencies meet the above-mentioned requirements lies with the parties (for mergers this has just recently been explicitly confirmed by the General Court in Deutsche Börse v Commission).

The same is true for the objective justification of an otherwise abusive behaviour under Article 102 TFEU – a concept that had been recognised in the case law of the Court of Justice for a long time but just recently (in the first Post Danmark case) has been explicitly aligned to an efficiency defence similar to the one under Article 101(3) or the Merger Regulation.

The reform of 2004, to conclude on this point, was actually never presented as an attempt to move merger assessment closer to the structure and standards applicable in antitrust, probably because antitrust was also evolving very rapidly at that time. But today, with a more than 10 years of perspective, this can be seen, without doubt, as a very positive consequence of that reform.

Influences of merger control on antitrust enforcement

Lets move now to examine this interaction between mergers and antitrust from the opposite perspective. How did merger control influence antitrust enforcement in the EU?

Market power analysis

It is perhaps not a coincidence that EU merger control developed in the same decade – the 1990s - as the effects-based approach in the area of antitrust. At that time, antitrust in the EU was moving away from form-based rules – such as the restriction of freedom of action – and towards the more economic approach introduced in the 1996 Green Paper on vertical restraints.

This more economic approach was essentially about taking better account of market power in the assessment of a given practice. That meant recognising that some vertical restraints were no longer hardcore (for example passive sales into another distributor's territory), and that non-block-exempted vertical restraints should be assessed in light of the parties' market power on their respective markets.

The new focus on market power in the area of antitrust benefitted from the experience developed by the Commission while dealing with market power in merger cases from 1990 onwards. In merger assessment the Commission acquired the reflex of looking at all relevant factors, not just a contractual clause in isolation. Concentration levels, barriers to entry, potential entry, entry and exit patterns, buyer power, capacity, growth, innovation, played an important role in merger control and where progressively imported in 101 and 102 analysis. Merger control contributed, therefore, to focus Articles 101 and 102 analysis on consumer harm and consumer welfare.

This development has also contributed to eliminating the “concentration privilege”, as it means that both mergers and agreements between competitors (unless restrictions by object) are not automatically considered anticompetitive but only if they are likely to result in consumer harm.

Market definition

To assess market power, you need a relevant market. And there again, merger control made a significant contribution. As you know, the Commission's current Market Definition Notice dates back to 1997. It was drafted largely on the basis of the experience gathered in the first 7 years of enforcement of the Merger Regulation. While some of its examples may now be a bit outdated, it continues to provide a solid methodological framework for both product and geographic market definition.

Many "object" cases under Article 101 do not require an assessment of the relevant market. But the Market Definition Notice has been used extensively in antitrust since 1997, especially in Article 102 cases, both in infringement decisions and in commitment decisions. Some antitrust decisions even refer to merger decisions as precedents about a particular market definition.

However, I should also add that market definitions in merger decisions should be taken "with a grain of salt" before they are imported into an antitrust case. First, the “cellophane fallacy” (according to which the hypothetical monopolist test cannot be applied to a market where prices are already above competitive level) is more likely to occur in antitrust cases than in merger cases. The Market Definition Notice recognises this point. Second, since antitrust is often about the past, we can often directly observe the parties' behaviour and deduce the relevant market from that, if needed. For example, a market-sharing agreement defines its own relevant market. In such cases, trying to further analyse the relevant market runs the risk of putting theory ahead of practical experience.

In fact, market definitions in merger decisions should be also taken "with a grain of salt" before they are "imported" into subsequent merger cases: our exercise of market definition is very much facts-driven and we stand ready to adapt our previous conclusions to the new prevailing circumstances, where markets have evolved, for instance by widening in scope.

Collective dominance

Collective dominance is another, and even clearer, "import" from merger control to antitrust. In the 1990s the leading antitrust judgment on collective dominance was *Compagnie Maritime Belge*. It stated that collectively dominant undertakings must "present themselves or act together on a particular market as a collective entity". Because there was so little case-law on collective dominance under Article 102, *Compagnie Maritime Belge* became the "standard" model: in that case, shipping companies "presented themselves" and "acted together" "as a collective entity" because they were bound by contractual links.

Then, in 2003, came the *Airtours* merger judgment. Already in the earlier *Gencor* judgment, the General Court had recognised that collective dominance can also occur when there are economic links between the parties. In *Airtours*, the Court ruled that there are three conditions for collective dominance based on economic links: (a) enough transparency to detect deviations, (b) credible retaliation, and (c) no sufficient competition from fringe competitors or buyer power. Two years later, the *Laurent Piau* judgment brought the *Airtours* case-law into the sphere of antitrust. Nowadays, collective dominance based on economic links, whether it is in antitrust or mergers, is based on the so-called *Airtours* test.[1]

In that regard, note that the section of the 2010 horizontal antitrust guidelines on information exchanges as an infringement 'by effect' set out an analytical framework which is very close to that for the assessment of collective dominance in mergers, as it refers to transparency, retaliation and fringe competitors and the customers' buyer power: this framework, as it is apparent, essentially coincides with the Airtours test.

[1] In the *Sony* judgment of 2008, the ECJ endorsed the General Court's *Airtours* test.

The counterfactual

Finally, the analysis of the "counterfactual" is another import from mergers to antitrust. In the past, some antitrust decisions took some shortcuts in this area. One could think of *European Night Services* and *O2 Germany*, for example – two Article 101 decisions that were annulled because in the absence of the agreement, the parties were not competitors in the first place.

In 2004, the Horizontal Merger Guidelines clearly stated that "[i]n assessing the competitive effects of a merger, the Commission compares the competitive conditions that would result from the notified merger with the conditions that would have prevailed without the merger." The counterfactual analysis in mergers relates thus to the issue of causality.

While the counterfactual test was always present in the area of antitrust – it was first mentioned in *Société Technique Minière* in 1966 – the prominent place of the counterfactual analysis in mergers since 2004 has raised its profile in the area of antitrust as well. The counterfactual test is now mentioned in all substantive guidelines on Article 101 and in the Guidance on Article 102, although I should add that according to the case-law, the counterfactual test only applies to Article 101 cases "by effect", not cases "by object". The latter seems obvious given the nature of the "by object" assessment. When two firms fix prices or share markets, it is hard to believe their argument that they were actually not competitors.

Is there (or should there be) a single analytical framework for Article 101 TFEU and merger control?

As a result of the mutual convergence processes between merger control and mergers that I have just described, numerous concepts and methodological approaches are today common to antitrust and merger analysis. Some have already been discussed, such as market definition and market power, single or collective dominance, the counterfactual, efficiencies or the effectiveness of a remedy.

Let me name a few others that are used identically or in a comparable way in the various Commission guidance documents (the Horizontal and Non-Horizontal Merger Guidelines as well as the Horizontal and Vertical Guidelines under Article 101 TFEU and the Enforcement Priority Paper under Article 102 TFEU):

- Anti-competitive effects have to be analysed in terms of parameters of competition (such as price, product quality or choice, innovation).
- The concept of competitor as including both actual and potential competitors.

- In order to be considered anti-competitive, a conduct or merger must be likely to produce harmful effects but no actual effects need to be proven.

- The various factors we take into account when assessing market power such as market share, concentration level, entry barriers, potential competition/entry and countervailing buyer power.

- “Safe harbours” (though there exact level is not identical under various guidelines).

- Horizontal effects of an agreement/concerted practice as well as a merger can consist in the loss of competition between the parties, reduced competitive pressure on third parties (absent coordination) or an increased coordination between market players (coordinated effects in mergers but also information exchange or commonality of costs through horizontal cooperation agreements).

- Vertical agreements or mergers are less likely to result in anti-competitive effects than horizontal agreements or mergers.

- The concept of anti-competitive foreclosure used in the analysis of vertical or conglomerate mergers, vertical agreements and exclusionary practices under Article 102 TFEU.

Finally, as regards the international dimension, the effects doctrine should be mentioned, according to which the EU has jurisdiction over conduct or mergers caused outside its territory that affect markets within the EU. The Court has endorsed this doctrine first in Woodpulp for antitrust enforcement and later in Gencor for merger control; now you find judgments quoting Woodpulp and Gencor at the same time.

On the other hand, two fundamental differences between merger control and antitrust remain:

- Merger control is about a prospective analysis of a future structural change in the market whereas antitrust enforcement addresses present or past market conduct.

- Hard-core restrictions and restrictions “by object” under Article 101 TFEU (which often, though not always, overlap) or “naked restriction” under Article 102 TFEU have no equivalent in merger control[2].

[2] Apart from the fact that the Horizontal Merger Guidelines indicate that efficiencies are unlikely to counterbalance the anti-competitive effects of a merger leading to a near-monopoly, see for instance Deutsche Börse/NYSE

In spite of these differences, when it comes to the respective assessment of horizontal anticompetitive agreements (leaving aside cases of restrictions by object) and horizontal mergers, the concepts of “restriction of competition” in Article 101 TFEU and of “SIEC” in Article 2 of the Merger Regulation are today, arguably, substantially similar and should result in the same level of intervention. Furthermore, as outlined above, both require a balancing of potential anti-competitive effects with likely efficiencies. While the fact that one of these tests is applied ex ante and the other normally ex post may undoubtedly be of practical relevance, it should have no bearing on the more conceptual question of whether or not both standards have actually converged.

Indeed, the Commission applied both tests to very similar competition problems, irrespective of the precise instrument used. For instance, when assessing the Oneworld, Star Alliance and Skyteam airline alliances under Article 101 TFEU, the Commission looked at closeness of competition between the parties, their combined market shares and barriers to entry and carried out a price concentration analysis based on economic data. It also analysed foreclosure effects potentially resulting from the parties restricting access to connecting traffic. All these elements, in turn, formed a decisive part as well of the analysis conducted by the Commission in airline mergers cases such as Lufthansa/Austrian, Ryanair/Aer Lingus or British Airways/Iberia.

This is even more evident in the assessment on joint ventures, and area where both merger control and antitrust play a significant role. The reason is quite simple: one the one hand, a joint venture results in the creation of a new legal entity and therefore changes the structure of the market. On the other hand, it creates a link between two or more firms – the parents – that otherwise remain independent market players.

Different systems of competition law have attempted to address this situation in different ways. Under German competition law, for instance, all joint ventures are subject to merger control but may likewise be assessed under Article 101 TFEU (or the equivalent provision of domestic law). The original EU Merger Regulation of 1989 created the famous dichotomy between “cooperative” and “concentrative” joint ventures: only the latter fell under merger control, all joint ventures where any type of cooperative effect under Article 101 TFEU could not be excluded where exclusively subject to the antitrust rules.

The 1997 reform of the Merger Regulation overcame this distinction. Since then, all “full-function” joint ventures are subject to merger control, irrespective of whether they may also give rise to coordination of the parents’ competitive behaviour[3]. It would be difficult to understand that, depending on the "full-functionality criteria", two very different substantive assessments would be applicable to joint ventures.

Actually, this is precisely an area where we can see how both instruments can be applied in a very similar manner. The BHP Billiton/Rio Tinto is a very good example. This case that was originally notified as a merger but, after a modification of the arrangements between the parties, it had to be subsequently assessed as an Article 101 case for lack of full-functionality. In this context, the Commission essentially carried out an analysis very similar to a merger one when applying Article 101 TFEU. No decision was however ultimately adopted, in so far as the proposed joint venture was abandoned by the parties in December 2010.

Conclusion

In sum, personally I would argue that, to a large extent, substantially the same test and standard of intervention apply in the context of antitrust and mergers, or to be more specific, in the assessment of agreements between competitors by effects under Article 101 and horizontal merger analysis in the EU. The assessment of restrictions by object under Article 101, which constitutes the majority of antitrust enforcement cases nowadays, follows, obviously, different standards.

As such, this convergence should not be particularly surprising. Merger control and antitrust enforcement address different forms of negative effects on competition, but they ultimately serve the same purpose: protecting competition and consumer welfare. Hence it is only natural that both instruments are based on many common concepts and methodological tools and that this convergence tends to increase over time.

A continued and enhanced dialogue between competition law enforcers and practitioners across instruments is useful to better understand the common concepts and objectives of both instruments, thereby strengthening the foundation of our antitrust and merger control work.

[3] However, the new Article 2(4) established that potential spill-over effects had to be analysed within the merger review procedure but under the analytical framework of Article 101(1) and (3) TFEU.