

The end of the SIEC test as a carte blanche for EU merger enforcement

- The General Court's Hutchison/O2 Judgment -

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Reactions from the antitrust world

"...promises to **rewrite EU merger control** in a similar way to *Airtours*" – David Parker, Director at Frontier Economics

"There are some **pretty harsh statements** that fault @EUCommission's overconfidence, as when the @Eucourt points out EC used a "relatively small sample" of ... 100 users (\$243)" – @CompetitionProf (Nicolas Petit, Professor at European University Institute, Twitter

"it was law vs discretion, and the **law won**" – Pablo Ibanez Colomo (Chair in Law at LSE, Visiting Professor at the College of Europe (Bruges)), *Chillin Competition*

"This **landmark judgment** represents a **significant setback** for Commissioner Vestager. Challenging four-to-three consolidation in the telecommunications sector has been a central feature of merger enforcement under her watch and the judgment will be studied closely to see the extent to which it may allow further consolidation in the sector." – Nicholas Levy, Partner, Cleary Gottlieb, quoted in the FT

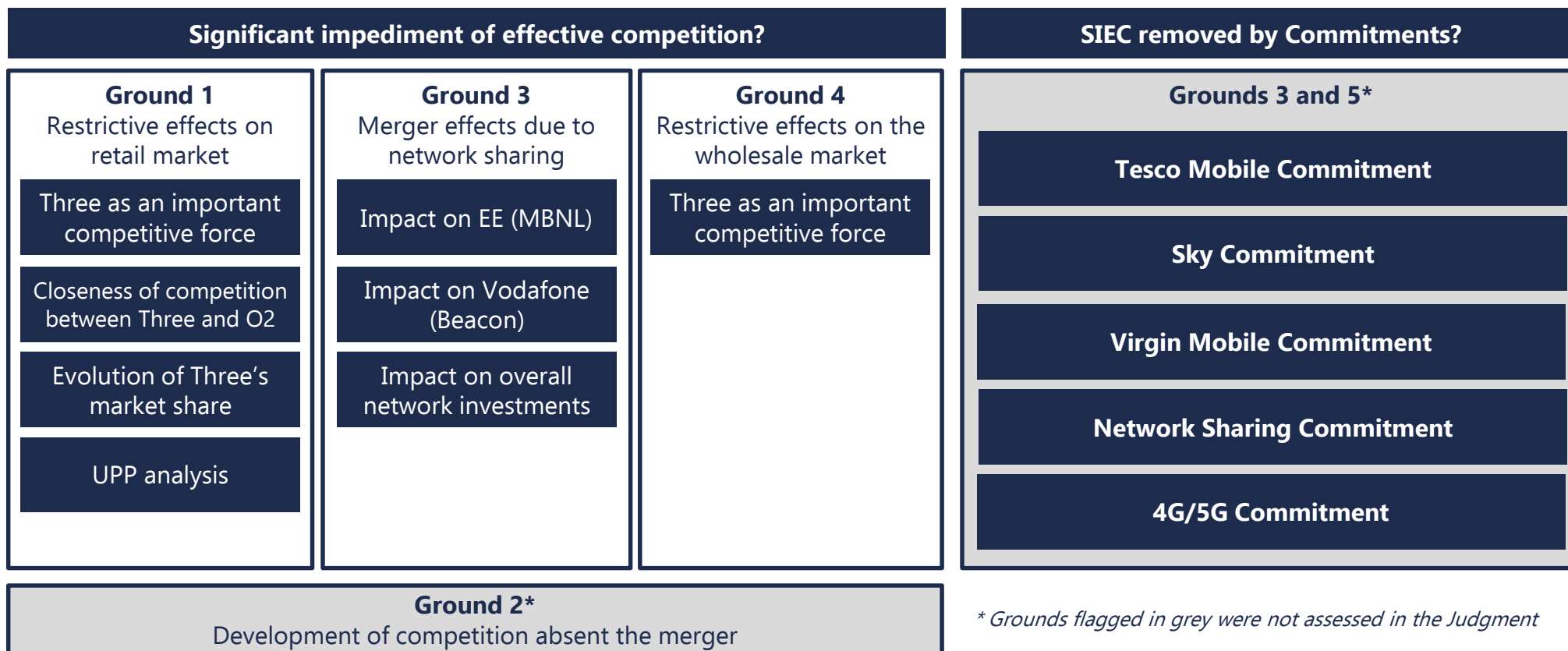
"...probably the **most important** [ruling that the court has issued regarding merger control in the past 15 years]... This is a **resounding victory** not only for CK Hutchison but for the entire European mobile telephony industry" – Douglas Lahnborg, Partner, Orrick, quoted in GCR

"**Ugly** for @EU_Competition. The General Court has just overturned the decision that blocked Telefonica UK & Hutchison 3G merger in the UK. **Broad swipe at the EU's analysis of the effects of competition.**" – @lewis_crofts, Editor-in-Chief, MLex, Twitter

"The judgment is, to be sure, of **major importance** for [the non-coordinated effects] aspect of merger control. It is **significant**, however, for **EU competition law at large.**" – Pablo Ibanez Colomo (Chair in Law at LSE, Visiting Professor at the College of Europe (Bruges)), *Chillin Competition*

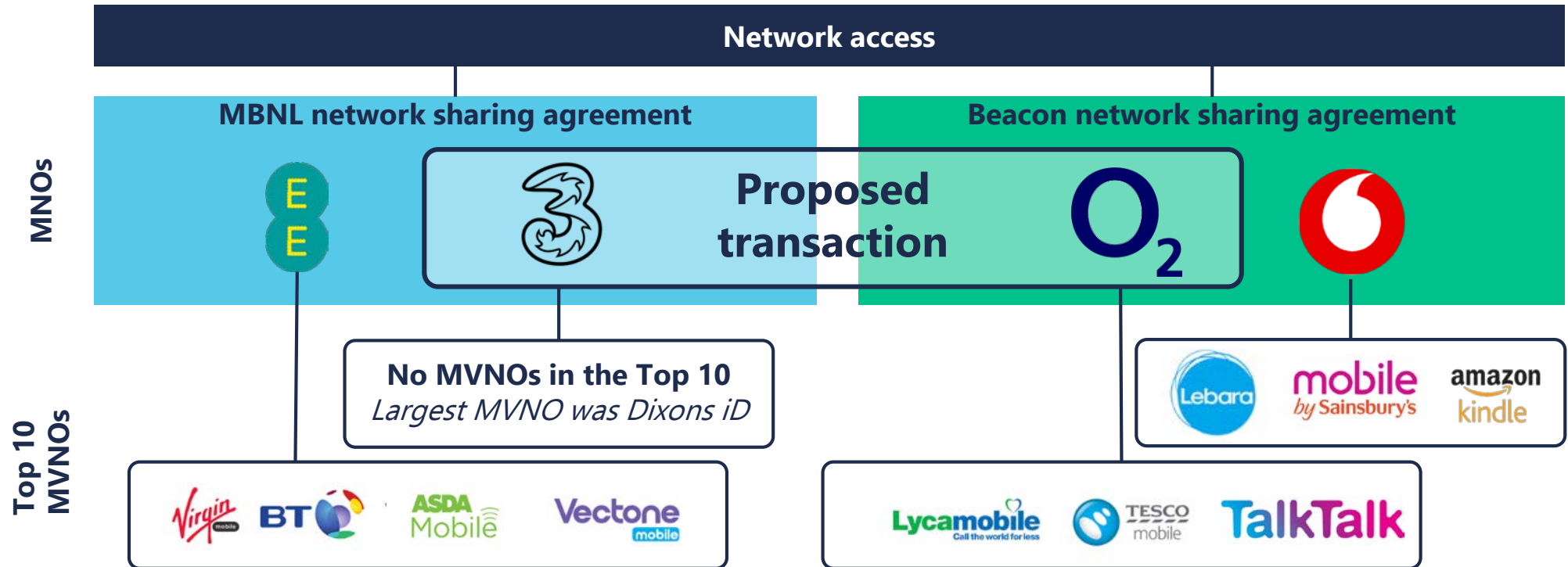
"[a] **shot across the bows** [of the antitrust regulators]" – Robert Grindle, Deutsche Bank, quoted in the FT

Grounds of appeal



** Grounds flagged in grey were not assessed in the Judgment*

The impact of the merger on network access arrangements



The General Court sends a signal



Experienced chamber – High quality bench of judges (First Chamber, Extended Composition), including President Marc van der Woude, previously a member of the Commission's legal service



M. Van der Woude (President), J. Svenningsen, E. Buttigieg, P Nihoul and U. Öberg (Rapporteur)



Ambitious judgment – Court requested detailed responses to written questions several weeks before the hearing and spent 2 days hearing the Parties' arguments and thoroughly scrutinising the Parties' pleadings

With the judgment the GC has confirmed that it intends to exercise full and rigorous review of Commission decisions

First judgment on the SIEC test

Key Messages given by the Court

The **threshold** for intervention was **not lowered** with the introduction of the **SIEC test** in the EUMR in 2004

An **ICF** must **stand out** from other competitors and merging parties must be **particularly close**

A finding of **closeness** or **ICF** alone may not be **sufficient** to justify a **SIEC** finding

UPP/GUPPI must show a **significant** price increase, taking into account **all relevant factors, including standard efficiencies**

Commission must perform an **overall significance assessment**

The bar is **higher** for **novel theories of harm markets** which require long term investment and must be **analysed over a longer period of time**

The SIEC test did not lower the threshold for Commission intervention



The changes made to the EUMR in 2004 were **not intended to lower the threshold** for Commission intervention in mergers – the **test** for intervention is the **same for when there is dominance**



The **standard of proof** for non-coordinated effects is the **same** as for coordinated effects (see *Airtours*)

"[The EUMR] must be interpreted as allowing the Commission to prohibit, in certain circumstances, on oligopolistic markets concentrations which, although **not giving rise to** the creation or strengthening of an individual or collective **dominant position**, are **liable to affect the competitive conditions on the market to an extent equivalent to that attributable to such positions** [...]"

Judgment, para. 90

"As the applicant correctly observed, the standard of proof applicable in order to establish that there are non-coordinated effects on an oligopolistic market is **not substantially different** from that applicable in order to establish coordinated effects. If that were not the case, the **Commission might classify the facts in such a way as to benefit from the most favourable rules of evidence** before the General Court."

Judgment, para. 109

A fundamental flaw: the Commission did not do enough to examine the **real probability** (as opposed to theoretical possibility) of any **competitive harm** from the merger.

Lack of overall assessment



“...that **global assessment is limited to a cursory reference** to the body of evidence and circumstances concerning, in particular, the elimination of an important competitive force by the concentration, the closeness of competition and the large market share of the merged entity, and which are thus aimed at demonstrating the existence of non-coordinated effects.”

Judgment, para. 288



“[i]rrespective of the probative value of that body of evidence and circumstances, it must be stated that the **Commission did not at any point specify** in the contested decision whether the non-coordinated effects identified would be ‘**significant**’ or **would result in the present case in a significant impediment to effective competition**, as it asserts in recital 1227 of the contested decision”

Judgment, para. 289

The Commission’s failure to conduct any overall assessment (in its 1,000-page long decision) is a **fundamental flaw** that affects the Commission’s entire SIEC analysis

General points on the legal standard



The **Court** is **not bound by the** Commission's Horizontal Merger Guidelines (**HMG**)

"While it is true that it is not necessary for the Commission to examine in every case all the criteria which it imposed on itself in the Guidelines, **nor has it been established that only one of those criteria is sufficient** to prove a significant impediment to effective competition, **in the absence of a detailed examination of the facts**"

Judgment, para. 447



While the Commission does not necessarily need to assess each factor from para. 26 of the HMG, it must **examine the facts in detail** and go beyond simply ticking one box to prove an SIEC

"The Court finds that the **reduction from four to three operators [...] is not, in itself, capable of establishing a [SIEC]** on the wholesale market in the present case. As is apparent from recital 25 of [the EUMR], **many oligopolistic markets exhibit a degree of competition which can be described as healthy.**"

Judgment, para. 434



There is **no presumption** of a SIEC in 4-to-3 mergers

"In the context of an analysis of a significant impediment to effective competition the existence of which is inferred from a body of evidence and indicia, and which is based on several theories of harm, the Commission is required to produce **sufficient evidence to demonstrate with a strong probability** the existence of significant impediments following the concentration."

Judgment, para. 118



Commission has to produce **sufficient evidence** to demonstrate with a **strong probability** the existence of a SIEC

The legal test for non-coordinated effects other than dominance

EUMR Article 2(3):

"A concentration which would significantly impede effective competition, in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position, shall be declared incompatible with the common market."

EUMR Preamble para. 25:

"elimination of important competitive constraints that the merging parties had exerted upon each other as well as a reduction of competitive pressure on the remaining competitors, may, even in the absence of a likelihood of coordination between the members of the oligopoly, result in a significant impediment to effective competition "

HMG para. 26:

Factors which may influence whether such effects are likely

Merging firms have large market shares

Merger eliminates an important competitive force (ICF)

Merging firms are close competitors

Competitors are unlikely to increase supply if prices increase

Merged entity able to hinder expansion by competitors

Customers have limited possibilities of switching supplier

Factors established in the Commission's decision

Factors not established in the Commission's decision



Assessment of non-coordinated effects in the retail market

Criteria for non-coordinated effects

The General Court assessed the following criteria in detail and found that the Commission made errors of law and assessment in respect of each:

- 1 ICF:** The Commission broadened the concept of an ICF so far that it would amount to a *de facto* prohibition of horizontal mergers in oligopolistic markets.
- 2 Closeness:** The Commission failed to show that the merging parties were particularly close.
- 3 Quantitative analysis:** Efficiencies must be taken into account in the Upward Pricing Pressure analysis.

“

“the **Commission’s application of the assessment criteria of the so-called ‘unilateral’ (or ‘non-coordinated’) effects** – namely, the concept of ‘important competitive force’, the closeness of competition between Three and O2 and the quantitative analysis of the effects of the concentration on prices – is **vitiated by several errors of law and of assessment**”

General Court press release

ICF – Confusing three separate concepts



Commission view:

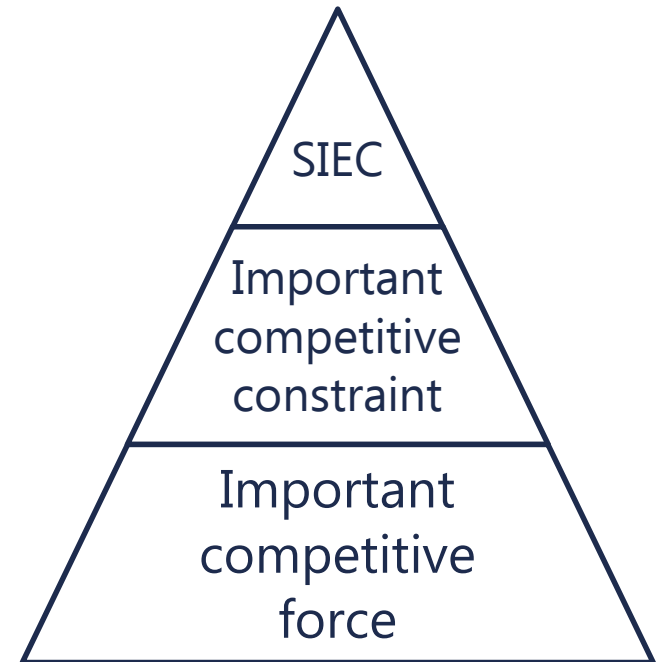
“...constitutes an important competitive force or, in any event it exerts an important competitive constraint – it is not required to conclude that either party constitutes an important competitive force”



“The approach taken by the Commission in the contested decision amounts in practice to **confusing three concepts...**”

“By confusing those concepts, the Commission considerably broadens the scope of Article 2(3) of Regulation No 139/2004, since any elimination of an important competitive force would amount to the elimination of an important competitive constraint which, in turn, would justify a finding of a significant impediment to effective competition”

Judgment, para. 173



ICF – Required to “stand out” from competitors



Commission view:

“contributes substantially and consistently to the competitive process”

“constitutes an important competitive force or, in any event it exerts an important competitive constraint – it is not required to conclude that either party constitutes an important competitive force”

“each MNO plays today a very important role in the competitive dynamic and constrains the others”



“The Commission’s assertion...that an important competitive force need not necessarily **stand out from its competitors in terms of its impact on competition** constitutes an error in law. Indeed, such a position would allow it to treat as an important competitive force any undertaking in an oligopolistic market, which would amount to a **de facto prohibition** on horizontal mergers in oligopolistic markets and would be a **breach of the principle of legal certainty.**”

Judgment, para. 158

“...the fact that the Commission determined that Three had **more of an influence on competition than its market share would suggest** is **not**, in itself, **sufficient** evidence to establish a significant impediment to effective competition in the present case.”

Judgment, para. 446

ICF – The probative value of gross add shares



The **absolute gross add share** of [10-15]% is **not sufficient** to establish an ICF, particularly in the context of much higher gross add shares in comparable mergers across Europe



The **delta** between market share and gross add share alone **cannot be sufficient** to find an ICF and a **small delta is no indicator** at all

"...gross add share which could be quantified, in this situation — most favourable to the Commission's case — with the highest growth rate, of approximately [between 10 and 20%], appears **very low and is not comparable** to the figures relating to new subscribers of the **undertakings that the Commission classified as 'important competitive forces' in its previous decisions...**"

Judgment, para. 186

| | T- Mobile / tele.ring (2005) | H3G Austria / Orange Austria (2012) | Telefónica Deutschland / E-Plus (2014) | H3G Ireland / Telefónica Ireland (2014) | H3G UK / Telefónica UK (2016) |
|---|------------------------------|-------------------------------------|--|---|-------------------------------|
| Gross add shares of smallest player in the market | > 50% | 33.1% | 20-30% | 21% | 10-15% |



ICF – Limited role for market shares



A combined market share of **37.5%** is **not indicative** of a SIEC

"The **combined market share** of the parties to the concentration of **37.5%** in 2015 is **not indicative** of the creation or strengthening of a dominant position in the present case or even, as such, of a **significant impediment to effective competition.**"

Judgment, para. 439



Prima facie, a concentration is less likely to have anticompetitive effects where one of the **merging parties has a particularly small** market share

"...a particularly **small market share** of one of the parties involved in the concentration **tends to suggest**, prima facie, an **absence of any significant impediment to effective competition**, especially where the other operators have much larger market shares"

Judgment, para. 437



In cases where one of the parties has a **small share**, the Commission has a **heightened burden** to demonstrate that the concentration would nevertheless lead to anticompetitive effects

"...the mere fact that Three's **gross add share is higher than its market share is not sufficient**, in the present case, to establish a significant impediment to effective competition, in a context where **Three's market share is, in actual fact, very small** and even its **gross add share**, on a market with only four operators, is **limited.**"

Judgment, para. 449



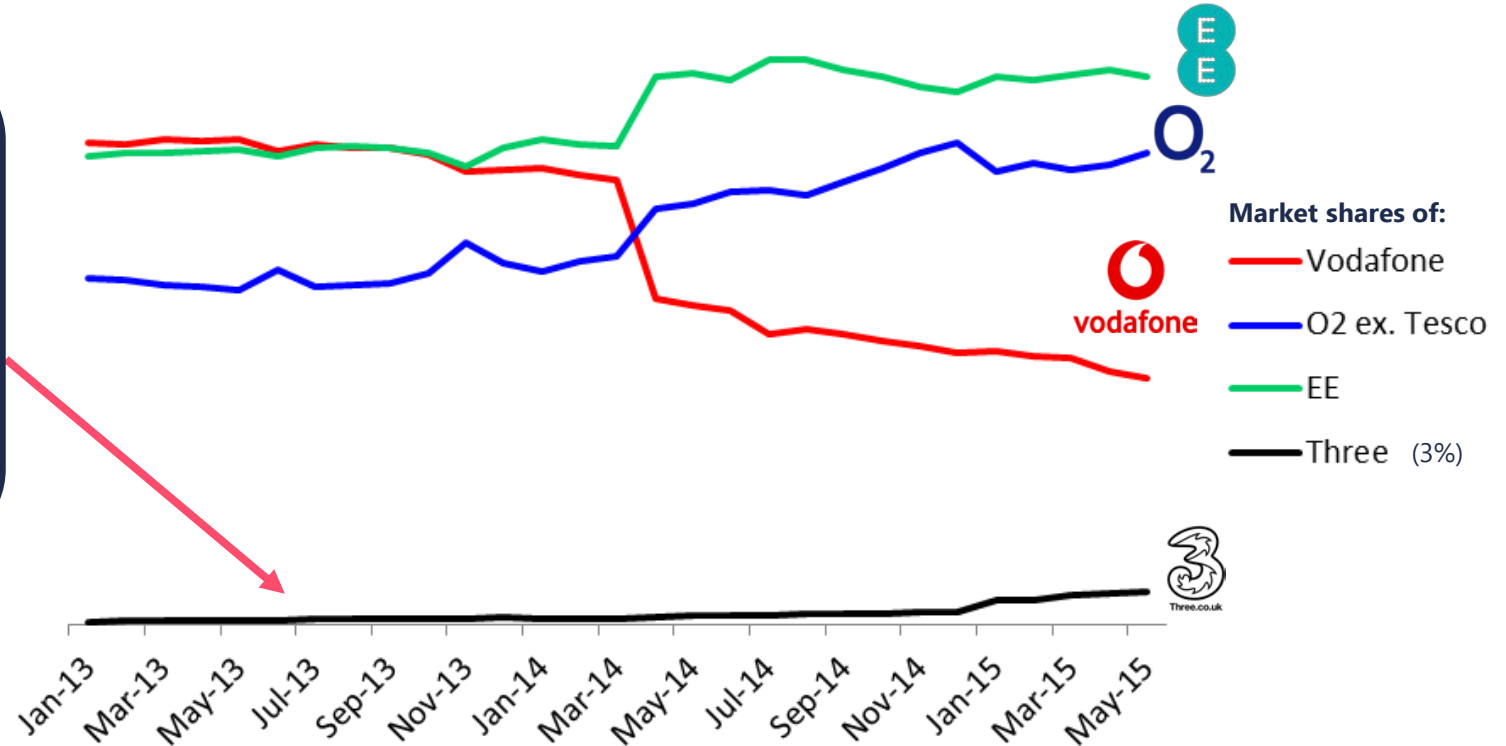
An ICF in the wholesale market...?

“

Commission view:

“...the Commission considers that Three constitutes an **important competitive force**...on the wholesale market”

Decision, para. 2295



* excluding Tesco Mobile
Source: Decision, Figure 125.

Closeness – Must be ‘particularly’ close

“

Commission view:

“Therefore, based on the results of the market investigation and the overall body of qualitative evidence in its file, the Commission considers that **Three and O2 compete closely with each other and the other MNOs**”

Decision, para. 438

Without denying the close competitive interaction that exist between the Parties, EE and Vodafone, the Commission preliminary considers that currently Three and O2 compete closely with each other. The **competitive pressure exerted by Three and O2 on each other is nothing but the demonstration of the vigorous competitive dynamic existing between MNOs in the retail market...**”

SO, para. 331

“

“Although it may indeed be established that **Three and O2 are relatively close competitors** in some of the segments of a concentrated market comprising four mobile network operators, **that factor alone is not sufficient** to prove, in the present case, the elimination of the important competitive constraints which the parties to the concentration exerted upon each other and **cannot suffice to establish a significant impediment to effective competition**; if that were not the case, any concentration resulting in a reduction from four to three operators would as a matter of principle be prohibited.”

Judgment, para. 249

Closeness – Which data is more reliable...?



“Third, the data used by the Commission to calculate the diversion ratios, which are used to analyse the degree of closeness of the various operators, are derived from a **survey** which it carried out on a **relatively small sample, of approximately 100 users**. Moreover, the results of that analysis do not tally with those of the quantitative analysis set out in Annex A to the contested decision. By contrast, **the ratios calculated by the applicant are based on MNP data and relate to 200 000 observations.**”

Judgment, para. 243

Quantitative analysis (UPP/GUPPI) – The probative value of forecasted price increases



UPP/GUPPI test always predict price increase and are **not credible forecasts** for **actual** price increases

“It is generally accepted that, while indicators of upward pressure on prices may be useful for screening purposes, by enabling the competition authorities to judge the need for a more thorough investigation, they must **not**, however, be regarded as **credible forecasts of price increases or simulations of mergers.**”
Judgment, para. 256



Forecasted price increases must be **significant**

“...even if the Commission had proved to the requisite legal standard in the contested decision that the concentration would be liable to encourage the merged entity to increase prices, and had quantified that price increase in the contested decision, the **Commission has not, in any event, demonstrated in the present case that the quantified price increase would be significant.**”
Judgment, para. 274



While there is no de minimis threshold, price increases must be forecast with a **sufficiently high degree of probability** and the Commission must take **all relevant factors** into account – including standard efficiencies

“Without there being any need to require the Commission to adopt a ‘de minimis’ rule or ‘safe harbour’ on price increases in the context of demonstrating the possible anticompetitive effects of a concentration, the Commission must, in any event, establish that increase with a **sufficiently high degree of probability.** When it decides to use quantitative analyses, such as those in Annex A to the contested decision, for that purpose, it must **take into account all the relevant factors** which may affect the price level.”
Judgment, para. 268

Quantitative analysis (UPP/GUPPI) – Efficiencies cannot be removed from the quantitative analysis

“

“The **Commission thus confuses two types of efficiencies**, namely those referred to in Section VII of the Guidelines and those specific to each concentration.

Efficiencies within the meaning of the Guidelines must be taken into account in the overall competitive appraisal of the concentration, in order to ascertain whether they are likely to **counteract the restrictive effects of the concentration.**”

Judgment, para. 279

“

“Moreover, the Court finds that it is apparent from the evidence submitted during the administrative procedure that, while a positive correlation may be established between concentrations which reduce the number of operators in the mobile telecommunications sector from four to three and result in price increases, a **correlation may also be established between those concentrations and an increase in network investments**...(see, in particular the Centre on Regulation in Europe (CERRE) Study by Genakos, C., **Valletti, T.**, Verboven, F., CERRE, Brussels, 2015)”

Judgment, para. 280



“

Commission view:

“... when assessing **efficiency** claims in merger investigation, the **Commission has so far never found that consolidation would significantly spur investment.**”

Commission Competition Merger Brief 3/2016 (Special Edition Telecoms), p. 2295

Assessing novel theories of harm



The burden of proof is higher for **novel** theories of harm

"...the **more prospective the analysis** is and the chains of cause and effect dimly discernible, uncertain and difficult to establish, the **more demanding the EU judicature must be in terms of the specific examination of the evidence produced by the Commission**"

Judgment, para. 332



The Court reminded the Commission that EU competition rules are designed to **protect competition, not competitors**

"EU competition rules are primarily intended to **protect the competitive process as such, and not competitors** ... [and] the fact that a concentration affects competitors is not in itself a problem. In particular, the **fact that rivals may be harmed because a merger creates efficiencies cannot in itself give rise to competition concerns**"

Judgment, para. 362



The Commission must take a **longer time frame into account** for the assessment of dynamic merger effects

"The Court finds that the analysis of the effects of a concentration on an oligopolistic market in the telecommunications sector which **requires long-term investment** and where consumers are often tied by contracts over several years is a dynamic prospective analysis which requires account to be taken of any coordinated or unilateral effects over a **relatively long period of time in the future.**"

Judgment, para. 415

Thank you

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