

Response to the CMA's Call for Information: Digital Mergers

1. In this submission, Simmons & Simmons LLP ("Simmons") provides some initial views on the questions posed in the CMA's Call for Information on digital mergers of 3 June 2019 (the "Consultation"), which is focused on amending the CMA's Merger Assessment Guidelines ("MAGs"). These are high level views based on concerns Simmons has heard from clients, as well as our monitoring of the discussion on this issue. We are very happy to go into more detail or have more involved conversations on any aspect following the CMA's initial review of this and other responses.
2. In summary, our views are as follows:
 - The CMA should engage in a more in-depth, expansive analysis of the potential for a digital markets transaction to reduce potential competition. However, such analysis must be based on concrete documentary evidence and economic data.
 - The CMA should be cautious of theories of harm involving innovation, both within and outside digital markets. Innovation is inherently difficult to predict and, as such, should the CMA block or impose remedies on a transaction based on a theory of harm relating to innovation, the CMA should face a higher evidentiary standard than it does for traditional theories of harm (such as high market shares, foreclosure etc.).

Questions

- (a) **What market features are likely to be relevant to the assessment of mergers in digital markets?**

For example:

- i. **The multi-sided nature of many digital markets (e.g. digital platform market)**
 - ii. **The way in which digital products or services are monetised (e.g. through advertising revenues)**
 - iii. **The fact that users in certain digital markets pay for products or services through non-monetary means (e.g. provision of personal data)**
3. Many users of "free" digital services now understand that they are, in effect, paying for such services by providing non-public data about themselves to the service provider (which will on-sell such data to advertisers). We do not view "paying with data" as objectionable in and of itself.
 4. The MAGs currently focus on price as opposed to other forms of currency. We believe the MAGs should be updated to discuss the potential of a merger to influence other forms of currency (including terms of data provision, see also response to question "(d)" below).
 - iv. **The relevance of data assets for competition**
 5. See response to question b(iii) below.

v. The importance of network effects

6. We believe that the MAGs, combined with the decisional practice of the CMA, already accommodate analysis for network effects.

(b) How might these market features impact the possible theories of harm?

For example

- i. Loss of actual or perceived potential competition (e.g. where the target is still relatively young but has growth potential, has promising pipeline products that have not yet come to market, or is currently only active in a complementary market).**
7. We believe that the CMA should certainly engage in an analysis of potential loss of a competitor in reviewing a merger concerning a new entrant or young company. However, we urge the CMA to be cautious and thoroughgoing in such an analysis. Both commentators and clients have expressed strong concerns about the CMA and other authorities being overly influenced by a backward-looking view of how digital markets have evolved.
8. Facebook’s acquisition of Instagram is often highlighted as a transaction that should have potentially been challenged on the basis that Instagram, left alone, would have grown and become a strong competitor to Facebook, particularly with respect to innovation.
9. However, such a backward-looking view and reliance on “gut feel” rather than economic evidence often ignores the counterfactual. Instagram is now a large social network with significant influence on the market, but at the time of its acquisition by Facebook in 2012, it had 13 employees, had never generated revenue and operated solely as a photograph-sharing site without any additional features. There was not a strong basis to block this transaction on an innovation theory of harm in 2012, and the CMA should resist the temptation to block acquisitions of small digital companies because of conjecture (that may be internal documents of the purchaser) of their potential to expand, particularly as such potential to expand may only be possible because of the combination.
- ii. Loss of innovation (e.g. where the market is characterised by competition in “innovation spaces” or the target has a history of disruptive digital innovation)**
10. Competition authorities have been increasingly focusing on the impact mergers may have on innovation in numerous sectors, not just digital markets. While we welcome the ability of the CMA to examine innovation issues, the MAGs should stress that innovation theories of harm can only be maintained if they are based on particularly robust evidence and data.
11. Innovation is inherently difficult to predict, including by companies active in a given industry. As such, their internal documents may reference certain innovation paths and pipelines that may never be realised (or at least deviate strongly from what does emerge). Accordingly, if the CMA prohibits transactions or demands remedies because there is some evidence that parties thought they would strongly compete on innovation with respect to products or services, this may meaningfully increase Type I errors (by preventing consolidation that would not have actually had a negative impact). Moreover, if the CMA has broad powers to intervene based on innovation theories of harm, this may facilitate the blocking of consolidations that would have by themselves

increased innovation (in other words, the over-extension of merger control intervention could harm markets by blocking harmless transactions, reducing the ability of these markets to innovate).

12. Our concerns with respect to innovation theories of harm also applies to digital markets – indeed, innovations are particularly hard to forecast in these markets, and they are incredibly fast moving.
13. We do not believe that innovation theories of harm should be unavailable to competition regulators, but the MAGs should stress that more evidence should be required to ground innovation theories of harm (as opposed to more traditional theories of harm such as high combined market shares and closeness of competition). This could be done in a similar way to how the MAGs distinguish between demand-side factors and supply-side factors, requiring a stronger case for the latter for it to be accepted.

iii. Non-horizontal effects (e.g. where the combined entity will control an important dataset for competition in upstream/downstream or neighbouring markets)

14. Data plays a complex role in many digital markets (acting as input, output and form of remuneration), but we do not consider that holding large amounts of data necessarily raises competition concerns. As has been noted by competition authorities that have examined consolidation of data, many datasets can be replicated and many others can lose their value quickly. Of course, if a combined dataset is protected by IP or less accessible because of technical barriers, the CMA should assess the combined entity's ability to control that dataset as they would any other input or essential facility.
15. Accordingly, we do not see amending the MAGs on this front as necessary.

(c) What other theories of harm might arise where the target is active in a complementary market?

For example:

- i. **Are there circumstances in which efficiency benefits arising from a merger could be considered to give rise to competition concerns?**
 - ii. **To what extent is it important to consider the possibility that a merger could prevent another firm from buying complementary assets and, as a result, be better able to compete?**
16. We believe many digital mergers can give rise to efficiencies. Often the simple combination of the right personnel (i.e., coders) can allow the creation of better digital products (similar to how the Commission recognised with respect the TomTom/Tele Atlas transaction that the vertical integration between a navigation systems provider and a digital maps developer would allow to deliver “better maps – faster” to the benefit of consumers).
 17. Against this background, we believe there would not be many instances in which digital mergers generate efficiencies but also do so in such a way that otherwise restricts competition (i.e., where the efficiencies themselves give rise to the problem). However, some such scenarios are possible – for example, if a large vertically integrated digital platform continued to purchase complementary assets, this may bring about efficiencies for consumers but at the same time prevent non-vertically integrated competitors from effectively competing at different levels of the distribution chain.

18. That said, the MAGs already provide that for efficiencies claims to be established, “*the efficiencies must be timely, likely and sufficient to prevent an SLC from arising*”. Accordingly, if a digital merger generated efficiencies but only at the expense of harm to competition, it would not meet the test already set out in the MAGs.

(d) How should we approach the assessment of non-price parameters of competition in digital markets?

19. As the CMA is aware, there are multiple parameters to competition, not just price. Given that many digital services are free for the user, providers typically compete on quality, network effects, and terms of usage (they compete more traditionally with price on the advertiser side of the market).

20. These parameters are already reflected in the MAGs, with the exception of terms of service. How a combination may impact terms of service may be unclear, but it could be the case that a target in a digital merger is a new entrant gaining a solid foothold based solely on the attractiveness of its terms of service (for example, it might have particularly strong privacy protections). If the purchaser in this case planned to change the terms of service to something less attractive for its users, this should be taken into account and, if the issue was severe enough, a behavioural remedy preventing the change could easily be imposed).

21. Accordingly, we recommend that Section 5 of the MAGs be updated to more clearly reference the potential for mergers to impact terms of service.

(e) When determining the counterfactual:

i. Which types of evidence should we take into account and how should these be weighted?

22. In line with the more general trend amongst competition authorities, we recommend that, in assessing digital mergers, the CMA prioritises assessing internal documents in a robust, holistic, and detailed manner. Many clients have raised concerns that regulators “cherry-pick” documents and do not arrive at conclusions based on looking at the available documents as a whole.

23. It is also important that the CMA assess documents in their correct context – often internal documents distort market realities for “sales” purposes (i.e., they exaggerate the strength of a business or its potential growth path). It is particularly important that the CMA be mindful of context with respect to any innovation theory of harm it is entertaining; many documents describing the potential innovation paths of a target are nothing more than educated guesses, and they cannot be treated as solid evidence unless heavily corroborated.

24. Any findings gleaned from the internal documents should be supported by robust economic data (although we recognise that highly detailed regression analyses are not feasible in many cases, the CMA’s conclusions should always have some grounding in credible data).

ii. How should we assess:

A. The growth prospects of the target

25. The CMA should be very cautious in assessing the growth prospects of the target. It may be exceptionally difficult to examine how a small target would develop as a potential competitor to the acquirer. As noted above, internal documents may be

unreliable sources on how and how much the target will grow. While we believe that analysis of the growth prospects of the target should form an important aspect of its SLC analysis for digital markets, the CMA must not resort to conjecture based on limited evidence. Instead, the CMA could consider engaging external consultants to comment on the growth prospects of the target if the available evidence is inconclusive.

- B. The availability of other routes for the target to grow (e.g. by attracting external financing)**
- C. The possibility of the target being acquired by an alternative party?**

26. The CMA can certainly take into account whether the target has other routes to grow, but it would likely be only of meaningful relevance in a scenario where it has already been established that an SLC would be likely because it appears the target will become a strong competitor to the purchaser. There would then be a question of whether the purchaser is the only player capable of growing the target (which would stand in favour of the purchaser) or if the target could naturally grow/be acquired by another party (in which case, this simply confirms a conclusion already reached on the target's prospects).

(f) What evidential weight should be attached to:

- i. Internal documents indicating that the purpose of the transaction is to eliminate a competitive threat?**
- ii. A high transaction value relative to the market value or turnover of the target?**

27. As noted above, internal documents represent a valuable source of evidence regarding the competitive effects of a merger, but they must be examined holistically and thoroughly. Moreover, other than in exceptional circumstances, they must be supported by solid economic evidence.

28. A high transaction value should be interrogated by the CMA, but not necessarily relied on as evidence (although, it can form corroborating evidence combined with internal documents and economic data). We accept that an unusually high transaction threshold for a small target could reflect a desire on the part of a purchaser to eliminate a competitor, but there could be a wide array of other, more benign explanations for high valuation (including, in the context of digital mergers, a desire to access complementary code or networks). Accordingly, transaction value should form part of the CMA's analysis, but it should not be determinative.

(g) Are there particular features of digital mergers that would be relevant to our assessment of efficiencies and relevant customer benefits?

29. As stressed above, digital mergers may give rise to substantial efficiencies, and these should be thoroughly assessed by the CMA. The MAGs currently provide valuable guidance on efficiency claims, but even on the terms of the MAGs such claims rarely succeed.

30. This is at odds with what is widely recognised by economists of differing viewpoints who point towards the many potential consumer welfare gains (aside from price) to be made from mergers.

31. Accordingly, we would suggest that the CMA, as a matter of policy, become more receptive to efficiency claims generally, including with respect to digital mergers.

(h) Are there any other aspects of the MAGs that should be supplemented or revised in relation to mergers in digital markets?

32. We believe the MAGs should be expanded to provide more detailed guidance on how non-problematic mergers can be identified and cleared quickly in phase 1. While the CMA is of course obliged to robustly investigate every transaction it reviews, many transactions which are quite clearly unproblematic (i.e., because there are no vertical or horizontal overlaps) are subjected to similar levels of scrutiny as potentially problematic transactions (i.e., the parties to these “safe” transactions are served with onerous requests to provide market data and other information that is ultimately not relevant).

33. Given that the Furman Report suggests that the CMA should be more “creative” with theories of harm in relation to digital markets, we are concerned that, without more clear guidance, many more non-problematic transactions could be subjected to inordinate regulatory processing, burdening both the relevant parties and the CMA. Accordingly, to better focus the CMA’s finite resources, the MAGs could include a “checklist” or rulebook on Phase 1 analysis that would allow the CMA to clear certain mergers quickly (e.g., mergers with no overlaps, relatively small parties, and/or no immediate evidence the acquirer’s attempt to “kill off” a nascent competitor).