EVERSHEDS SUTHERLAND

CMA CONSULTATION ON THE CMA'S DRAFT REVISED MERGERS ASSESSMENT GUIDELINES

EVERSHEDS SUTHERLAND'S RESPONSE

1. Introduction

1.1 Eversheds Sutherland (International) LLP welcomes the opportunity to comment on the CMA's consultation on its revised Mergers Assessment Guidelines (CMA129 CON) ("**Draft Revised Guidelines**").

1.2 We confirm that this response does not contain any confidential information and we are happy for it to be published on the CMA's website.

2. Executive summary

2.1 An update to the current Merger Assessment Guidelines ("**Current Guidelines**") has been long-awaited, and the publication of the Draft Revised Guidelines which reflect a number of developments to the CMA's approach to merger control is welcomed.

2.2 The CMA's enhanced role going forward post-Brexit in combination with its jurisdictional thresholds (and how these can be interpreted), means that it is important for merging companies to have as much clarity and certainty as possible as to how the CMA will approach the substantive assessment of mergers. Whilst the Draft Revised Guidelines bring about greater certainty in some respects, there are some areas where further clarity would be welcomed, and we have highlighted these below.

2.3 As a general point, we note that the Draft Revised Guidelines state that the CMA may make findings (including the finding of an SLC) despite uncertainty or a lack of evidence. Such an approach is likely to lead to considerable uncertainty from the perspective of merging parties and risk "false positives". In addition, such an approach appears to place a lower evidential burden on the CMA than it does on merging parties, which in our view, is problematic.

2.4 We note that on a number of occasions the Draft Revised Guidelines refer to the CMA's provisional findings in some of its cases as the underlying precedent. We would caution against an over-reliance on provisional findings of the CMA which have not been fully tested through the entirety of the CMA's merger investigation process.

2.5 We set out below a number of other practical and substantive points that we believe could be usefully addressed or clarified in the Draft Revised Guidelines.

3. Comments and observations: Mergers - the CMA's jurisdiction and procedure: CMA2

Chapter 2 – A substantial lessening of competition

3.1 We note that a number of paragraphs in this chapter indicate that the presence of uncertainty or an absence of evidence will not preclude the CMA from finding an SLC (see, for example, paragraphs 2.10, 2.26, 2.27 and 2.28(c)). This is concerning as it appears that the evidential standard that must be satisfied by the CMA is considerably lower than that which must be satisfied by merging parties. In addition, such an approach is likely to generate considerable uncertainty from the perspective of merging parties.

Non-price factors

3.2 Paragraph 2.5 of the Draft Revised Guidelines makes reference to non-price aspects of competition, and advises that terms such as "quality" should be interpreted broadly (for example, to include the level of privacy offered to users of digital services, the sustainability of a product or service, and the ability to enjoy content without being served with advertisements).

3.3 We agree that particularly in digital markets, firms compete on parameters such as level of privacy and lack of advertising, and that elements such as these are relatively straightforward metrics to identify, define and measure. Other non-price parameters such as sustainability, however, are potentially more nebulous, and the Draft Revised Guidelines would benefit from further guidance on how parameters such as these are likely to be identified and measured by the CMA. In our view, there is a risk that a broad definition of "quality" may extend merger investigations and competition law more generally into areas which may be more appropriately dealt with through other areas of the law (e.g., privacy law or environmental law). It is therefore important for the scope of parameters such as this to be appropriately defined.

Market share benchmarks

3.4 We note that the Draft Revised Guidelines do not make any reference to a market share benchmark for undifferentiated products (i.e., the 40% market share benchmark in paragraph 5.3.5 of the Current Guidelines has been removed). We appreciate that shares of supply are less important where there is less of a focus on market definition / shares of supply and more of a focus on closeness of competition. In our view, however, it is nonetheless helpful for businesses for the Revised Guidelines to refer to shares of supply which are likely to give rise to substantive concerns, even where it is understood that such benchmarks are indicative and should not be applied mechanically.

Internal documents

3.5 We note the CMA's increased reliance on internal documents in recent years which is recognised in the Draft Revised Guidelines. In paragraph 2.24, there is recognition that the CMA may attach different weight to different evidence including internal documents depending on the circumstances. While it may not be appropriate to explicitly mention COVID-19 in the Draft Revised Guidelines, we note that it seems likely that certain categories of internal documents created prior to the pandemic are of limited evidential value going forwards.

3.6 We also note the CMA's comments at paragraph 2.27 of the Draft Revised Guidelines that it may be more reliant on internal documents in mergers in fast-moving sectors where other types of evidence may be more limited (i.e., where there is a lack of evidence of how the market has developed over time). It is worth noting that, in this case, the parties' internal documents are also likely to be speculative, and so it is vital that the CMA takes into account that context when undertaking their assessment and determining what weight to attach to those documents.

3.7 Finally, we note the comment in paragraph 2.9 of the Draft Revised Guidelines that "*a lessening of competition may also be considered substantial where the lessening of competition is small, but the market to which it applies is large or otherwise important to UK customers*", with a footnote to *J Sainsbury's Plc/Asda Group Ltd*. stating that the CMA had regard to the fact that groceries were a non-discretionary expenditure that accounted for a significant share of household spend. It would be useful if the Draft Revised Guidelines could expand on any other markets or categories of markets which may be considered important to UK consumers.

Chapter 3 – The counterfactual

3.8 As a general point, the removal in the Draft Revised Guidelines of limb 3 of the failing firm test (which considers what would have happened to the sales of the firm in the event of its exit) is a welcome development. In our view, this part of the test is unclear and difficult to apply, and we agree that it should not form part of the test going forward.

3.9 The Draft Revised Guidelines expressly state at paragraph 3.3 that "*the CMA's conclusion on the counterfactual does not seek to ossify the market at a particular point in time*" and at paragraph 3.15 that "*the time horizon the CMA considers when describing the counterfactual will depend on the [market] context*". In our view, this is a welcome acknowledgement of the need to take a dynamic approach to the counterfactual, particularly when it comes to digital markets.

3.10 The Draft Revised Guidelines no longer refer to the CMA's approach to parallel transactions (when considering a "competing bids" scenario). Guidance on this point appears at paragraphs 4.3.25-4.3.27 of the Current Guidelines. In our view, it may be helpful for the Draft Revised Guidelines to make clear whether the CMA intends to consider parallel transactions in its counterfactual assessment going forward.

3.11 The Current Guidelines at, for example, paragraph 4.3.6 state that "*when it considers that the choice between two or more scenarios will make a material difference to its assessment, the [CMA] will carry out additional detailed investigation before reaching a conclusion on the appropriate counterfactual*". This statement is not replicated in the corresponding part of the Draft Revised Guidelines (paragraph 3.13). The counterfactual is a key building block for the CMA's analysis and our experience is that it can be important for the CMA to undertake a detailed investigation of alternative counterfactuals in some cases. In a context where the CMA wishes to undertake a dynamic assessment of competition in its merger investigations (which we agree with) our view is that it is important to retain this language to ensure that the CMA continues to investigate the counterfactual in detail in those cases where that is required.

Chapter 4 – Horizontal unilateral effects

3.12 We note that section 5.9 of the Current Guidelines on countervailing buyer power has not been replicated in the Draft Revised Guidelines, and is instead replaced with two paragraphs on the subject (paragraphs 4.18 and 4.19). It is unclear why the Draft Revised Guidelines do not include an in-depth section on countervailing buyer power, and there is a risk that this omission will lead to uncertainty on the part of merging parties who wish to raise countervailing buyer power arguments.

3.13 Paragraph 4.19 of the Draft Revised Guidelines states that "*most other forms of buyer power that do not result in new entry – for example, buyer power based on a customer's size, sophistication, or ability to switch easily – are unlikely to prevent an SLC that would otherwise arise from the elimination of competition between the merger firms*." It is unclear why buyer power based on a customer's size, sophistication, or ability to switch easily is unlikely to prevent an SLC from arising, and the Draft Revised Guidelines would benefit from explaining this. In addition, the Draft Revised Guidelines fail to make clear that buyer power resulting in the expansion of existing competitors (i.e., not just new entry) can also prevent an SLC from arising.

3.14 We welcome the expansion on the Current Guidelines' discussion on two-sided markets. In our view, however, it is not necessarily the case that "*network effects mean that mergers among platforms are more likely to give rise to competition concerns*" (see paragraph 4.24 of the Draft Revised Guidelines), and the CMA should exercise caution in applying this blanket presumption in all cases.

3.15 Paragraph 4.31 of the Draft Revised Guidelines states that in cases where the CMA would have to consider a large number of local overlaps between merger firms, it may employ a filtering approach. Whilst there is some guidance in paragraph 4.31 as to how the CMA might apply such a filtering approach, in our view it is important that the CMA takes a consistent approach towards this across cases in order to ensure that there is as much certainty as possible for merging parties.

Chapter 5 – Potential competition

3.16 As a general point, it is to be welcomed that the Draft Revised Guidelines cover potential competition in considerably greater detail than the Current Guidelines, including the introduction of a section on loss of future competition, which is reflective of the CMA's recent decisional practice. In addition, the departure from the concepts of "actual potential competition" and "perceived potential competition" is a positive development as these were unclear, and as per the consultation document, often caused confusion with merging parties.

3.17 We note that on a number of occasions throughout this chapter, the Draft Revised Guidelines either suggest or make clear that uncertainty or a lack of evidence does not preclude the CMA from making a particular finding. By way of example, paragraph 5.15

of the Draft Revised Guidelines states that the acquisition of a potential entrant may be concerning "*even if its impact is uncertain, or expected to be small*". Similarly, paragraph 5.20 states that "*uncertainty about the outcome of a dynamic competitive process does not preclude the CMA from assessing the impact of the merger on that dynamic process*". Finally, paragraph 5.23 makes clear that the CMA may find an SLC even where entry by an eliminated entrant is "*unlikely and may ultimately be unsuccessful*".

3.18 The low evidential burden that the CMA sets itself in this regard is concerning, particularly in light of the high thresholds which the Draft Revised Guidelines impose on parties to transactions (for example, if merging parties wish to successfully rely on countervailing constraints from entry and/or expansion by third parties, the Draft Revised Guidelines state that the CMA "*must be satisfied*" that rivals will have both the ability and incentive to enter or expand (paragraph 8.32). In our view, the same evidential standard should apply to both the CMA and merging parties. In addition, if the CMA is able to make findings despite uncertainty or a lack of evidence, this inevitably leads to uncertainty from the perspective of merging parties, and the possibility of findings based on "false positives", which is clearly undesirable.

Chapter 6 – Coordinated effects

3.19 In paragraph 5.5.9 of the Current Guidelines, it is clear that all three of the conditions as set out in paragraphs 5.5.9(a)-(c) must be satisfied in order for a finding of coordination to be possible.

3.20 The equivalent paragraph in the Draft Revised Guidelines, paragraph 6.10, simply states that "*the CMA will analyse the extent to which the following three conditions are met*", but does not make clear whether it is still a requirement for all three of the conditions to be satisfied in order for a finding of coordination to be possible.

3.21 Similarly, the wording of paragraphs 5.5.9(a)-(c) of the Current Guidelines makes clear that it is a requirement for each condition to be satisfied (i.e., "*firms **need** to be able to reach and monitor the terms of coordination*", "*coordination **needs** to be internally sustainable among the coordinating group…*" and "*coordination **needs** to be externally sustainable…*" (emphasis added)). This is not reflected in the wording of paragraphs 6.10(a)-(c) of the Draft Revised Guidelines.

3.22 In our view, the Draft Revised Guidelines should therefore make clear upfront that it is still the case that all three conditions must be met, or otherwise explain why the CMA's position has changed in this regard.

Chapter 7 – Vertical and conglomerate effects

3.23 The Draft Revised Guidelines are helpful in providing more detail on the framework that the CMA will adopt and the three main foreclosure theories of harm it will examine when conducting its analysis of vertical and conglomerate effects arising from mergers.

3.24 We welcome the additional examples provided by the CMA of the mechanisms through which a merged entity could potentially harm its rivals when supplying inputs and agree that the CMA should focus on understanding if these mechanisms would allow the merged entity to foreclose its rivals, rather than predicting the actions the merged entity might take.

3.25 The Draft Revised Guidelines also helpfully expand the list of costs and benefits that the CMA will consider when examining whether a merged entity will have the incentive to foreclose its rivals. We also welcome the clarification made in the Draft Revised Guidelines that as long as sufficient credible downstream rivals are left unaffected by the actions of the merged entity, then foreclosure of some marginal competitors may not harm competition.

3.26 We welcome the additional guidance from the CMA that conglomerate effect concerns may be greatest in nascent and digital markets, as new customers may be more easily diverted between firms and competitors more easily marginalised. We agree that in such markets

the anticompetitive effects may not emerge in full until the market has reached maturity (as was the case with *Facebook/Instagram*) so the CMA should focus its assessment on the impact to structure of the market and competition over the longer term. However, it would be helpful if the CMA could provide greater insight into the approach it will take in conducting such an analysis and the types of information it is likely to ask parties to a transaction to provide.

Chapter 8 - Countervailing factors

Efficiencies

3.27 We welcome the CMA providing a more detailed framework for how it will conduct its assessment of efficiencies that will arise as a result of a transaction, particularly in relation to the requirements that any efficiencies claimed must "enhance rivalry" and "benefit consumers".

3.28 The Draft Revised Guidelines make clear that whilst the CMA does not take relevant customer benefits into account as part of its competitive assessment, it may do so when considering whether to make a Phase 2 reference or when considering remedies. It is helpful that the Draft Revised Guidelines confirm that the CMA generally views reduction in marginal or variable costs as more effective in enabling firms to make price reductions or quality improvements than a reduction in fixed costs. These clarifications are both consistent with our recent case experience.

3.29 However, when compared to the Current Guidelines, the Draft Revised Guidelines provide less guidance and explanation on the types of efficiencies that will be considered as part of its assessment. It would be helpful if the CMA provided more information on the specific types of efficiencies it will consider persuasive, particularly in relation to digital markets.

Entry and Expansion

3.30 We note that it is made explicit in paragraph 8.26 of the Draft Revised Guidelines that the CMA considers that entry and/or expansion preventing an SLC from arising would be rare. The CMA appears to be particularly concerned that an analysis of its past cases has shown that on occasion, when it has relied on entry or expansion to clear mergers, that entry or expansion did not in fact materialise.

3.31 The very nature of a "realistic prospect" and "balance of probabilities" standard of proof is that some likely events do not, in practice, materialise, and in our view, this is not a reason in and of itself to set such a high standard for proof of entry and expansion. In addition, the source relied upon by the CMA to support its argument that in some instances where it relied on entry or expansion to clear mergers, such entry and expansion did not materialise is a report carried out by KPMG in 2017 which was commissioned by the CMA. This report is based on evidence from only eight merger cases from 2009-2015, selected from a list of cases recommended by the CMA, and is therefore limited. In our view, such a report should not be relied upon to support such a high standard for proof of entry and expansion.

3.32 Whilst the Draft Revised Guidelines provide further detail on the framework that the CMA will engage when determining whether entry or expansion would prevent an SLC from arising, they provide less clarity than the Current Guidelines on the specific types of information that the CMA will gather when assessing potential entry or expansion. It would be helpful if the Draft Revised Guidelines were expanded to include the types of evidence that the CMA will consider during its case assessment, particularly in relation to nascent and digital markets.

Chapter 9 - The market in which an SLC arises

3.33 While the CMA is required under the Enterprise Act 2002 to identify the market or markets within which an SLC will arise as a result of a transaction, and we agree that it is an important part of the overall merger assessment process, in our view it is positive that

the Revised Proposed Guidelines place less importance on this stage of the CMA's analysis than is the case in the Current Guidelines.

3.34 The Revised Proposed Guidelines are consistent with our experience from recent years in noting that the CMA places less emphasis on market definition and greater significance is given to information gathered by the CMA as part of its competitive assessment, such as from internal documents, bidding history, customer and competitor feedback etc. We agree that this is more likely to reflect the competitive dynamics of a market accurately rather than relying on market share data. As such, we welcome the CMA's suggestion that it will take a "simple approach" towards defining the market.

3.35 However, bearing in mind the CMA's approach that it will not normally have regard to market share and concentration thresholds calculated on anything other than the narrowest market that satisfies the hypothetical monopolist test, we consider that it would be useful for the Draft Revised Guidelines to provide more information on the types of evidence and information that the CMA will consider during this process to enable lawyers to better advise clients ahead of a CMA investigation.