SLAUGHTER AND MAY

Slaughter and May response to CMA consultation: Draft revised Merger Assessment Guidelines (CMA129 CON)

1. Executive summary

1.1 We welcome the opportunity to provide feedback on the CMA's revised Merger Assessment Guidelines (the "**Revised Merger Guidelines**"). The CMA's approach to merger assessment has evolved considerably in recent years and revising the guidelines to bring them into line with the CMA's prevailing practices is therefore a valuable exercise.

1.2 Similarly, the CMA's proposal to align its approach to "exiting firm" counterfactual scenarios with the approaches of other leading competition authorities is welcome, as is the recognition of environmental benefits as a potential source of efficiencies.

1.3 However, there are a number of areas where the Revised Merger Guidelines should, in our view, be amended prior to publication to ensure consistency with the prevailing legal framework and/or to ensure the Guidelines are of maximum value for businesses, their advisors and the CMA's case teams. We highlight the following in particular:

(i) **Approach to the SLC test is not in line with case law**: The Revised Merger Guidelines suggest that a lessening of competition may be considered "*substantial*" when it is "*more than trifling*". This is not supported by applicable case law or legislation.

(ii) **Omission of benchmarks indicating a lack of competition concerns**: The Revised Merger Guidelines omit previous guidance on the scenarios in which the CMA (and its predecessors) considered that competition concerns were typically *unlikely* to arise. These have been replaced with additional guidance on scenarios that may give rise to an SLC, most of which are at the "upper end" of the spectrum of cases that may give rise to competition concerns. These examples are of less use for self-assessment purposes. We would encourage the CMA to reinstate the previous examples of scenarios that are unlikely to give rise to competition concerns, particularly as the economic intuitions underpinning those scenarios remain unchanged.

(iii) **Asymmetric treatment of uncertain future events**: There is growing asymmetry in the CMA's approach to similar future events: for example, the low threshold for establishing entry by a merging firm for the purposes of constructing the counterfactual as compared to the conditions for countervailing entry by a third party. Such disparities do not appear to us to be justified.

(iv) **Downplaying the role of efficiencies**: By codifying the CMA's scepticism of efficiency claims, the Revised Merger Guidelines will dissuade merging firms from advancing credible arguments, creating a self-fulfilling prophecy. Similarly, the suggestion that synergy claims may be used as evidence of a firm's incentive to enter a market organically will further deter efficiency claims, and appears to be

founded upon a simplified view of the way that commercial investment decisions are taken.

1.4 We would be happy to discuss the points raised in this paper further with the CMA if helpful. Please contact Anna Lyle-Smythe (anna.lyle-smythe@slaughterandmay.com) or Alex Bulfin (alex.bulfin@slaughterandmay.com).

2. Context for revisions: alleged under-enforcement

2.1 The Revised Merger Guidelines purport to respond to a trend in "*under-enforcement, particularly in relation to digital markets*". The CMA cites the Furman and Lear reports as evidence that changes to the Merger Assessment Guidelines are needed to address suspected under-enforcement, and notes that it has "*carefully considered (and largely adopted)*" the findings of those reports in the Revised Merger Guidelines. [1]

2.2 However, the debate around whether, and to what extent, there has in fact been under-enforcement in relation to digital mergers is more nuanced than this premise suggests. The general observation, drawn from the Furman report, that the five largest digital firms have collectively made over 400 acquisitions globally with no prohibitions and "*very few*" conditional clearances does not necessarily imply that any of those deals ought to have been blocked or been subject to remedies. The Furman report acknowledged that "*most acquisitions made by digital companies are likely to be benign or beneficial to consumers due to efficiencies, and the potential for innovative products and services to be brought more quickly to market*";[2] this observation was also recently endorsed by the Digital Markets Taskforce in relation to acquisitions by firms with strategic market status.[3] The ex-post assessments conducted by Lear of some of the high-profile digital mergers approved in recent years is also more nuanced than the consultation documents might suggest.[4] It should also be acknowledged that it is the prospect of potential acquisition by a larger firm that often drives innovation efforts by start-ups and SMEs (a point acknowledged in the Furman report).[5]

2.3 Even if it were accepted that there has been historic under-enforcement in relation to digital technology mergers, this does not necessarily justify a general change in approach affecting other sectors. The recent advice of the Digital Markets Taskforce to the UK government on the design and implementation of a new pro-competition regime for digital

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[1] *Ibid*, para. 1.7-1.8.

[2] *Unlocking digital competition: report of the Digital Competition Expert Panel* (March 2019) (the "**Furman Report**"), para. 1.110.

[3] "[T]he majority of mergers by firms with [strategic market status] are likely to be competitively benign (and will often have significant benefits for consumers." *A new pro-competition regime for digital markets: advice of the Digital Markets Taskforce* (CMA 135), December 2020, Appendix F, para. 4.

[4] For instance, the report notes that "[t]he decisions taken in *Facebook/Instagram* and *Google/Waze* may have represented missed opportunities for the emergence of challengers to the market incumbents but have also likely resulted in efficiencies. The decisions taken in *Priceline/Kayak* and *Amazon/The Book Depository* appear less controversial, as the level of competition in the markets concerned does not seem to have been substantially affected by the mergers." Lear*, Ex-post Assessment of Merger Control Decisions in Digital Markets* (9 May 2019), p.xiii.

[5] The Furman Report, para. 1.157

markets already includes proposals for a new merger regime for digital firms with strategic market status, including a reduction in the standard of proof at Phase 2 from the "balance of probabilities" standard to the "realistic prospect" standard currently used at Phase 1. Against that backdrop, it is unclear that extensive changes to the Revised Merger Guidelines, ostensibly to address (perceived historical failings in the review of) mergers in digital markets, are needed.

2.4 The CMA has also acknowledged in the Revised Merger Guidelines that its role and the legal tests it applies remain unchanged, and that recent developments in certain sectors (in particular those stemming from digital technologies) have not introduced new theories of harm or economic principles in the field of merger control.[6] There is a tension between this acknowledgement and the CMA's assertion that changes are needed to address under-enforcement. If the CMA feels that the legal and economic framework in which it has been operating has been insufficient to allow enforcement against certain transactions in digital markets, we suggest that this needs to be addressed through legislative change rather than by adjustments to non-binding guidelines.

2.5 Finally, we note that little consideration appears to have been given in the consultation documents to the risks of over-enforcement. Indeed, in many cases the CMA seems to proceed from the starting point that mergers are unlikely to generate any specific benefits for consumers that could not have been achieved through other means (see further 10.2 below). Yet the objectives of many mergers are expressly pro-competitive, including reducing costs, realising economies of scope or scale, or responding to changes in technology and emerging consumer preferences. Deterring pro-competitive, or competitively benign, mergers deprives consumers of the resulting benefits; a point acknowledged by the Digital Markets Taskforce.[7] The Revised Merger Guidelines should therefore explicitly recognise the risks of both under- and over-enforcement.

3. Purpose of the Revised Merger Guidelines

3.1 The stated primary purpose of the Revised Merger Guidelines is to assist merger firms and their legal and economic advisers.[8] The CMA has acknowledged that it is "*crucial that the CMA provides appropriate guidance to businesses entering into transactions which may have an impact on competition in the UK*".[9] We agree with this focus.

3.2 However, for guidance to be effective, it must be capable of practical application. Particularly in the context of the CMA's voluntary notification system, merging firms and their advisers need clear, practical guidance so that they can determine with reasonable accuracy the CMA's likely assessment of any proposed transaction. The absence of such guidance increases the burden (in terms of time, cost and risk) faced by businesses trying to anticipate the likelihood and nature of any substantive concerns the CMA might have

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[6] Revised Merger Guidelines, para. 1.4.

[7] See footnote 3.

[8] *Draft revised Merger Assessment Guidelines – consultation document* (CMA129 CON), 17 November 2020 (the "**Consultation Document**")

[9] Revised Merger Guidelines, para. 1.3.

regarding a particular transaction. In turn, this both discourages potentially pro-competitive transactions while also encouraging the defensive notification of unproblematic mergers (placing a disproportionate administrative burden on the CMA).

3.3 In our view, the Revised Merger Guidelines do not currently meet these requirements.

(i) **Importance of addressing both pro- and anti-competitive factors:** The Revised Merger Guidelines tend to focus on factors and avenues of enquiry which are likely to result in the CMA finding a potential SLC, without addressing factors that may indicate an absence, or a reduced risk, of an SLC.[10] The latter is equally important if merging firms are to judge where their merger sits on the spectrum of transactions that may or may not give rise to substantive competition concerns. Examples include:

(a) Portraying synergy claims as a potential source of evidence that a firm might have had an incentive to enter a market absent the merger, while largely dismissing the potential for efficiencies to offset an SLC finding. See further Section 10 below;

(b) Suggesting that while the CMA is not required to quantify an SLC, "*any direct* [quantitative] *evidence that price increases, deteriorations in non-price competitive parameters or losses of innovation would occur as a result of the merger may be considered as evidence that the merger is likely to give rise to an SLC*", without acknowledging that the contrary ought also to be true (for instance where estimates of post-merger price increases suggest that any merger-specific effect on price will not be substantial and/or may be outweighed by efficiency gains); and

(c) Placing increased emphasis on the potential for vertical mergers involving large downstream customers to enable customer foreclosure strategies while marginalising the role of buyer power as a countervailing constraint in horizontal mergers.

(ii) **Removal of benchmarks**: Previous iterations of the Merger Assessment Guidelines provided useful indications of circumstances which (in light of the experience of the CMA's predecessors) were less likely to give rise to substantive competition concerns.[11] It is well understood by businesses and their advisors that such benchmarks are non-binding, are not to be applied mechanistically, and do not limit the CMA's discretion to fully investigate cases falling within/below those thresholds. This has not in any way diminished their usefulness. The CMA has acknowledged that the legal and economic framework in which it operates is unchanged, and we would therefore expect these benchmarks to remain

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[10] See, for example, Revised Merger Guidelines, para. 2.17.

[11] See, for example, *Merger Assessment Guidelines* (CC2 (revised) / OFT1254), September 2010 (the "**2010 Guidelines**"), para. 5.3.5, which indicated that mergers would not often give rise to concerns where: combined market shares are below 40%; at least four firms would remain in the market post-merger; or the increment to HHI would be below 250 (in a concentrated market) or 150 (in a highly concentrated market).

relevant.[12] We would encourage the CMA to follow the approach of its predecessors and reinstate guidance as to the scenarios in which competition concerns are less likely to arise (based on the CMA's experience).[13] This would help businesses and their advisors better assess where their transaction lies along the full spectrum of cases considered by the CMA.

3.4 In addition to providing crucial guidance to businesses, the Revised Merger Guidelines ought to provide a template for the analytical framework adopted by case teams, particularly at Phase 1. This should ensure a higher degree of internal consistency and rigour in the CMA's approach to investigation and decision-making. This function of the Revised Merger Guidelines should be expressly acknowledged in the text itself.

4. Approach to the SLC test

4.1 The Revised Merger Guidelines correctly reflect the finding of the Competition Appeal Tribunal in the *Global Radio* case that "*substantial*" does not necessarily mean "*large*", "*considerable*" or "*weighty*".[14] However, the Revised Merger Guidelines also state that substantial "*is capable of meaning* 'not trifling' *at one extreme and* 'nearly complete' *at the other*". This risks misapplying judicial precedent regarding the interpretation of "*substantial*" and represents an immediate appeal-risk for the CMA.

(i) The House of Lords has confirmed that "*as a matter of common language*" (emphasis added), the word "*substantial*" accommodates a wide range of meanings, from "*not trifling*" at one end of the spectrum to "*nearly complete*" at the other. However it did not endorse the notion that the meaning of "substantial" for the purposes of the jurisdictional test under the Fair Trading Act 1973 (the "**1973 Act**") should be located at the lower extreme of that spectrum (i.e. that it should be equated to a "*more than de minimis*" standard).[15]

(ii) To the contrary, Mustill LJ concluded that, in the context of the 1973 Act, the meaning of "substantial" lies "*further up the spectrum*". As a general indication of where the meaning of the word lay, without trying to impose a precise definition, Mustill LJ used the expression "*worthy of consideration for the purposes of the Act".* Indeed, the judgment goes as far as to *"accept the respondent's submission that if the* [Monopolies and Mergers Commission] *proceeded when examining its*

[12] "[T]*he CMA's role and the legal tests that it applies remain the same*" (Revised Merger Guidelines, para. 1.4) and "[the changes in the CMA's approach to merger control] *have not introduced new theories of harm or economic principles*" (Consultation Document, para. 1.4).

[13] The inclusion of a new list of illustrative scenarios where an SLC may arise (at para. 2.17) is not a sufficient substitute. Businesses are still left without any meaningful guidance as to where the lower bound of the spectrum of cases that may give rise to competition concerns should be located.

[14] *Global Radio Holdings Limited v Competition Commission* [2013] CAT 26.

[15] *R v Monopolies and Mergers Commission ex parte South Yorkshire Transport Ltd* [1993] 1 WLR 29. The CMA appears to accept, by its reference to this judgment, that the interpretation of the word "substantial" should be given the same meaning under the Enterprise Act 2002 as under the 1973 Act, which is consistent with the CAT's findings in the *Global Radio* judgment.

jurisdiction on the basis that it was enough for the reference area to be more than trifling this was a radical misconception" (emphasis added).[16]

4.2 In a similar vein, no justification is given for the CMA's suggestion that "*where the evidence supporting* prima facie *competition concerns is stronger, especially if there is little evidence to the contrary, at an early stage, the CMA will expect to undertake less detailed analysis in deciding whether there is an SLC*" (emphasis added).[17] Irrespective of the timing and sequence in which it receives evidence, the CMA should be considering all inculpatory and exculpatory evidence in the round when deciding whether there is an SLC, to the requisite evidential standard. The fact that the early evidence may tend in one direction does not relieve the CMA of its statutory duty to establish whether the test for reference is met to the requisite standard overall. The CAT has also recently emphasised the CMA's duty to make proper inquiries as to the availability of relevant evidence, even at a late stage in the investigative process.[18]

4.3 We also note that "*evidence to the contrary*" in the above context means evidence of an absence of an SLC; this risks giving the impression that the burden of proof is reversed in circumstances where the CMA has found *prima facie* evidence of competition concerns at an early stage of its investigation, which is not supported by legislation or precedent.

4.4 The Revised Merger Guidelines also state that "*a lessening of competition in a market (or in a particular segment of a market) may be considered substantial even if that segment or market is small in total size or value.*"[19] The CMA could assist businesses and their advisors by providing practical guidance as to what is likely to constitute a "small" market or segment in this context, or when a lessening of competition may be of sufficient seriousness to result in an SLC finding in relation to such a market. We note that the Revised Merger Guidelines could usefully cross-refer to the CMA's guidance on *de minimis* markets (while acknowledging that the question of whether an SLC may arise is distinct from the question as to whether there is an exception to the duty to refer).[20]

4.5 The Revised Merger Guidelines also suggest 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 is otherwise important to UK customers*".[21] There is no obvious economic basis for this assumption, and there is similarly a lack of practical guidance as

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[16] *Ibid*.

[17] Revised Merger Guidelines, para. 2.18.

[18] *JD Sports Fashion plc v Competition and Markets Authority* [2020] CAT 24. The European Courts have made similar findings regarding the duty of the European Commission to consider the information available to it, including potentially relevant information which could have been obtained, upon the Commission's request, during the administrative procedure, in the context of State aid investigations: see Case C-300/16 P *European Commission v Frucona Kosice A.S.* (20 September 2017), paras. 70-71.

[19] Revised Merger Guidelines, para. 2.9.

[20] *Mergers: Exceptions to the duty to refer* (CMA64), 13 December 2018, para. 7 et seq.

[21] Revised Merger Guidelines, para. 2.9.

to what constitutes a "large" market or a market of importance to UK customers. The Revised Merger Guidelines could provide further guidance in this regard.

5. CMA's approach to evidence

5.1 The Revised Merger Guidelines correctly reflect the CMA's increasing reliance on the merging firms' internal documents in merger investigations, and its use of deal valuations as a source of evidence. That these familiar aspects of the CMA's practice are now expressly acknowledged in the Revised Merger Guidelines is welcome.

5.2 However, the value of internal documents can only be properly understood when they are interpreted in light of the business context in which they were created. Internal documents may be created by individual employees motivated by a range of strategic and personal considerations, not all of which will align with, or be representative of, the objectives or true incentives of the firm or its management. Similarly, documents created by investment banks and external consultants may be influenced by considerations other than those directly related to the firms' rationale for pursuing a deal, and any statements regarding market conditions (even those reproduced in internal papers) should be given more limited weight given the authors' relative lack of in-depth market knowledge.

5.3 There can also be a tendency among case teams, particularly at Phase 1, to focus on allegedly unhelpful statements contained in the merging firms' documents and to disregard or attribute little weight to statements that support the parties' case. Aspects of the Revised Merger Guidelines appear to implicitly endorse such an approach, in particular when assessing prospective market entry by the merging firms (see 8 below).

5.4 The Revised Merger Guidelines could helpfully provide merging parties with assurances that the CMA will review documents in a holistic manner, which means both the avoidance of "cherry-picking" particular phrases, pages and documents (while excluding others) and ensuring that documents are interpreted in their proper commercial context in order to give them appropriate weighting.

5.5 The Revised Merger Guidelines could also provide useful guidance on the circumstances in which the CMA will likely request additional internal documents beyond those specified in sections 8-10 of the Merger Notice. Such guidance would allow merging firms to identify documents of potential interest at an earlier stage, making pre-notification more efficient.

6. Counterfactual

6.1 We are concerned that the consultation documents downplay the significance of the counterfactual.[22] The counterfactual establishes the baseline against which a merger's potential effects ought to be assessed: as the CMA notes, "the appropriate counterfactual may increase or reduce the prospects of an SLC finding by the CMA".[23]

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[22] Consultation Document, para. 1.32.

[23] Revised Merger Guidelines, para. 3.2.

6.2 The 2010 Guidelines sought to balance the uncertainty inherent in prospective merger analysis with the need to establish a proper baseline for assessment of a potential SLC. They did so by incorporating into the counterfactual only those events or circumstances, and their consequences, that are "reasonably foreseeable" while retaining the discretion to consider the effects of more uncertain events as part of the competitive assessment.[24]

6.3 By contrast, the Revised Merger Guidelines omit all reference to "reasonable foreseeability" and instead indicate that the CMA will embrace a greater degree of uncertainty when establishing counterfactuals. As a preliminary point, we note that firms engaged in the market may find themselves wrong-footed in their assessment of the way in which a market may develop. The CMA - without the same depth of market knowledge - should proceed with extreme caution when making assumptions about uncertain future market developments. This is particularly true of fast-moving digital markets, where predicting future market developments is most challenging.

6.4 More fundamentally, the approach advocated in the Revised Merger Guidelines would give the CMA considerable scope when setting the counterfactual to imply a higher level of competition than the prevailing market conditions would otherwise suggest, thereby increasing the prospect of an SLC finding. The Digital Markets Taskforce has implicitly acknowledged that market uncertainty may limit the CMA's ability to find an SLC in digital markets, and that changes to the statutory regime are required to address this problem. If that is the case, the CMA ought not to be able to achieve the same ends by adjusting the way it approaches the counterfactual, without any change to the underlying legal framework.

6.5 We are particularly concerned at the suggestion that the CMA may consider "*the ability and incentive*" of the merging firms to pursue alternatives to the merger as part of the counterfactual. This appears to open the possibility for the CMA to extrapolate merging firms' commercial strategies in order to construct a supra-competitive counterfactual scenario, even in the absence of explicit supporting evidence.[25]

6.6 In our view, the Revised Merger Guidelines would afford the CMA too much latitude in the construction of its counterfactual (in circumstances where the CMA is already afforded a wide margin of appreciation in its competitive assessments) and implicitly lowers the bar for finding an SLC. In line with the approach described in the 2010 Guidelines, we consider that the counterfactual should be constructed on the basis of reasonably foreseeable events, with more uncertain developments assessed, in the round, as part of the competitive assessment.

6.7 We also suggest that the wording of paragraph 3.10 of the Revised Merger Guidelines be amended to make clear that the CMA is unlikely to assess in depth any significant changes affecting competition from third parties <u>as part of the counterfactual</u>, but that any

[24] 2010 Guidelines, para. 4.3.2.

[25] Revised Merger Guidelines, para. 3.14. We also note the suggestion at footnote 61 of the Revised Merger Guidelines that the CMA may use the merging firms' valuation of revenue synergies as evidence of their incentives to pursue organic expansion. As further explained in Section 8 below, the fact that entry/expansion might be profitable does not mean that a firm will choose to pursue that strategy.

such developments would nevertheless be considered as part of the competitive assessment (in line with the statement made at paragraph 3.21).

6.8 We welcome the decision to omit the third limb of the exiting firm scenario, bringing the Revised Merger Guidelines into line with the approach taken in other jurisdictions.

6.9 We also welcome the clarification that at Phase 1 the CMA "*will not engage in a comparative analysis of multiple competing bids*".[26] The Revised Merger Guidelines should further clarify that the CMA will not find that there is a realistic prospect of an SLC arising at Phase 1 on the basis that a transaction that does not otherwise give rise to substantive concerns may be less pro-competitive than an acquisition by an alternative purchaser.

7. Horizontal unilateral effects

7.1 Mergers in concentrated markets: The CMA's assertion that "*where competition mainly takes place among few firms, any two would likely be sufficiently close competitors that the elimination of competition between them would raise competition concerns, absent evidence to the contrary*" is at odds with the recent judgment of the EU's General Court in the *Hutchinson/O2* case.[27] As the General Court rightly observed, the presumption that any competitor in an oligopolistic market constitutes an important competitive force would allow a competition authority to prohibit any horizontal merger in such markets without proper analysis of the competitive constraint that the merging firms exert upon one another.[28] While the EU and UK legal frameworks are not identical, the economic insight underpinning the General Court's judgment is nevertheless relevant in the UK context. The CMA has sought to align other aspects of the Revised Merger Guidelines more closely with other leading competition agencies around the world (see 6.8 above); neither the Revised Merger Guidelines nor the Consultation Document explains why the CMA considers a different approach is merited in relation to mergers in oligopolistic markets.

7.2 Buyer power: The Revised Merger Guidelines limit the application of countervailing buyer power to situations of sponsored entry and self-supply, with limited supporting analysis for this change.[29] Such an approach is too narrow and does not reflect commercial reality. In certain sectors, customers may represent the most significant constraint on a firm's ability to increase prices, worsen quality, range or service or reduce innovation (see, for example, the role of supermarkets as a key route-to-market for suppliers of fast-moving consumer goods). Failing to account for these effects in the competitive assessment would represent a significant omission. The explanation put forward in the Revised Merger Guidelines (that market power and buyer power are two sides of the same coin) is too simplistic; firms may interact with customers across a range of markets, and an increase in market power in one area may have little, or no, impact on the overall balance

[26] Revised Merger Guidelines, para. 3.34.

[27] Case T-399/16 *CK Telecoms UK Investments v Commission* (26 June 2020).

[28] *Ibid*, para. 173-175.

[29] Revised Merger Guidelines, para. 4.19.

of bargaining power between parties. The CMA is able to speak to the merging firms' customers as part of its investigation, and could therefore adopt a more nuanced approach to assessing the interactions between buyers and suppliers in a given market (where this is merited by the facts of the case), rather than focusing exclusively on sponsored entry and self-supply.

7.3 Two-sided markets: The Revised Merger Guidelines suggest that an SLC may occur where a merger accelerates the market towards tipping, as customers are deprived of the benefits of a longer period of competition between platforms vying to be the winner.[30] We note however that any loss of interim competition must nevertheless be sufficiently substantial to meet the statutory test: this should be recognised expressly in the Revised Merger Guidelines. The Revised Merger Guidelines should also acknowledge that in these circumstances potential efficiencies (e.g. economies of scale) would be realised sooner than would be the case if the market were left to tip organically.

7.4 More generally, the Revised Merger Guidelines could provide greater clarity as to how the CMA will identify markets that are prone to tipping, beyond stating that this is more likely in markets exhibiting network effects. By way of example, the Revised Merger Guidelines do not acknowledge that network effects can also lead consumers to swiftly abandon a platform, or that tipping is less likely to occur where customers are willing to multi-home. The Revised Merger Guidelines should contain more nuanced guidance to help businesses identify when their transaction involves markets which the CMA may regard as prone to tipping, and could draw further upon the useful discussion of the features of digital markets contained in the Furman report.[31]

7.5 Local mergers: It is unclear how the description of the CMA's approach to local mergers in the Revised Merger Guidelines should be reconciled with the CMA's existing commentary on retail mergers.[32] For example, the *Retail Mergers Commentary* contains references to indicative thresholds (e.g. that combined market shares of less than 40% will not often give the CMA cause for concern over unilateral effects) which have been omitted from the Revised Merger Guidelines (see 3.3(ii) above).

8. Potential competition

8.1 The Revised Merger Guidelines suggest that the CMA may rely on its assessment of a firm's economic incentive and ability to enter or expand into a given market, even in the absence of any evidence of an explicit intention to do so.[33] The proposed approach risks undermining the CMA's approach to the proper use and weighting of available evidence. As the CMA notes in the discussion of countervailing entry by rivals, "*in some instances, when* [the CMA] *has relied on entry or expansion to clear mergers, that entry or expansion*

[30] Revised Merger Guidelines, para. 4.24(a).

[31] E.g. The Furman Report, para. 1.65 *et seq.*

[32] CMA's *Retail Mergers Commentary* (CMA62), 10 April 2017.

[33] Revised Merger Guidelines, para. 2.28(c), 5.11 and 5.12.

did not in fact materialise".[34] First, this highlights the perils inherent in speculating on future entry and expansion. Second, it demonstrates the inconsistency of the CMA's approach to dealing with entry by merging firms as opposed to third parties. It is unclear that such divergent approaches to similarly uncertain market developments is justified.

8.2 Moreover, the fact that it may be profitable for a firm to enter a given market does not mean that it fits with the firm's corporate strategy or perception of how the market may develop, nor that the firm would consider entry to be the best use of its limited resources and capital. The absence of any explicit intention to enter or expand into a given market within a foreseeable period should be taken as strong *prima facie* evidence of a lack of potential competition. The approach outlined in the Revised Merger Guidelines could effectively require the merging firms to "prove a negative" in order to rebut the CMA's entry hypothesis, and risks shifting the burden of proof from the CMA to the merging firms.

8.3 Even where a firm has previously articulated an intention to enter or expand into a given market, it is not necessarily the case that this intention remains. Just as the CMA has cited prospective entry by rivals that did not materialise, there are many examples of firms assessing, and even investing in, potential entry or expansion which ultimately did not come to fruition, either because it proved not to be feasible or it was ultimately not considered to be in the firm's commercial interest. Some firms will routinely re-assess opportunities for entry and expansion, but this does not mean that such entry or expansion is a strategic priority or would in practice be considered the best use of a firm's limited resources (see further 10.2(ii) below).

8.4 More generally, factors such as barriers to entry and likelihood of success (which are discussed in the context of countervailing entry)[35] ought to be relevant to, but are missing from, the discussion of entry by one of the merging firms in the context of establishing the counterfactual and potential competition. We would encourage the CMA to cross-refer to these factors when discussing prospective entry by the merging firms.

8.5 With regard to paragraph 5.20 of the Revised Merger Guidelines, we suggest clarifying that the degree of uncertainty of success within a dynamic competitive process is nevertheless relevant to assessing the strength of the competitive constraint exercised by the firms involved. For example, in markets with a high degree of uncertainty of success, firms with a strong track-record of successful research and innovation may be regarded as a more credible sources of future competition than firms with comparably weaker track-records.

9. Vertical and conglomerate effects

9.1 The 2010 Guidelines recognised that "*it is a well-established principle that most* [non-horizontal mergers] *are benign and do not raise competition concerns*", while

[34] Revised Merger Guidelines, para. 8.26. Regarding this observation, we note that in the context of countervailing entry, the question ought to be whether the threat of entry would be sufficient to offset a post-merger increase in prices or reduction in quality, service, range or innovation efforts. The threat of credible entry might pose a sufficient constraint on the remaining firms in the market, without the need for actual entry: i.e. lack of entry could equally signify that the CMA's reliance on countervailing entry was in fact justified.

[35] *Ibid,* para. 8.38.

nevertheless noting that in certain circumstances such mergers may give rise to an SLC.[36] The Revised Merger Guidelines omit such a statement. The CMA has acknowledged that the Revised Merger Guidelines do not reflect the introduction of new theories of harm or economic principles; given that the economic intuitions underlying the original statement remain unchanged, we would expect this principle still to be reflected in the Revised Merger Guidelines.

9.2 Similarly, the CMA states that "*a number of commentators continue to warn of the substantial risks of under-enforcement against vertical mergers*", but in support of this cites only two journal articles and one example of alleged under-enforcement (concerning Google's acquisition of DoubleClick in 2007, which was subject to an in-depth Phase 2 review by the European Commission at the time) which the CMA identified as part of its digital advertising market study.[37] Again, it is not clear that one historic, alleged instance of under-enforcement justifies the change in tone evident in the Revised Merger Guidelines, and any decision to move away from established economic principles should be underpinned by a robust body of evidence.

9.3 Finally, the suggestion that the CMA may focus on qualitative, rather than quantitative, assessment of incentives in complex and dynamic markets represents a significant shift from the approach outlined in the 2010 Guidelines, and risks introducing uncertainty into the assessment.[38] Qualitative evidence may usefully illustrate a firm's incentives in some circumstances, but should not be regarded as substitutable for a proper economic analysis of a firm's incentives to foreclose its rivals. The CMA has not provided examples of cases where the quantitative analysis of incentives failed to identify problematic vertical mergers, and which might have been addressed had a qualitative approach been employed. For the reasons discussed above, we would also caution against reliance on internal documents in isolation to assess a firm's incentives.

10. Countervailing factors - Efficiencies

10.1 The CMA's position that "*it is rare for a merger to be cleared on the basis of countervailing factors*" is a self-fulfilling prophecy.[39] The CMA's scepticism towards efficiency arguments is widely understood by businesses and their advisors. Consequently, few businesses would embark upon a transaction for which the CMA's acceptance of countervailing efficiencies would be a pre-requisite for clearance. Even where such claims are well-founded, firms and their advisors are likely to be reluctant to pursue them given the CMA's stance. As a result, it is unsurprising that the CMA does not have much experience of clearing mergers on efficiency grounds, and the inclusion of such a statement in the Revised Merger Guidelines effectively ensures that such claims will rarely, if ever, be advanced.

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[36] 2010 Guidelines, para. 5.6.1.

[37] Revised Merger Guidelines, para. 7.6 and footnote 110.

[38] Revised Merger Guidelines, para. 7.17.

[39] Revised Merger Guidelines, para. 8.1.

10.2 We are particularly concerned by the suggestion that substantial efficiencies may "*imply that merging firms would have considerable incentive to realise these* [efficiency] *claims through other means in the absence of the merger*"; this risks becoming detached from the commercial reality of investment decisions.

(i) Generating comparable efficiencies organically may require far greater time and investment (e.g. to build assets and infrastructure or to recruit personnel) than would an inorganic acquisition. Organic strategies (such as investment in R&D) may also involve a much greater degree of uncertainty in terms of success compared to acquiring an existing solution.[40] A merger may allow the firms to generate efficiencies and pass these on to consumers faster and at a reduced cost, freeing up capital to be deployed in other areas of the business;

(ii) Businesses do not have infinite resources and therefore do not consider investment opportunities in isolation. A firm's corporate strategy is likely to involve ongoing consideration of myriad opportunities for expansion and investment, with management choosing how to deploy a firm's limited resources so as to secure the best return. The projected return on an acquisition may not be much more than the projected return on an equivalent organic strategy, but nevertheless could be sufficient to convince management to pursue growth in this area of the business compared to a wholly separate division;

(iii) The CMA's suggestion that licensing agreements, buying groups and contractual agreements may allow firms to realise efficiencies without a merger does not take account of the shortcomings of such alternatives. Such arrangements typically do not allow a firm to influence materially the direction of its partner's future commercial or innovation strategies. Not only would the firm thus assume greater commercial risk (through increased dependency on a third-party supplier),[41] but it is also likely to be more difficult to realise the full benefit of potential synergies through, for instance, full alignment of future innovation plans. In certain circumstances, these alternative business arrangements will also give rise to additional competition law risks, the management of which is likely to impose an additional compliance burden on the firms involved: for instance, the time and cost involved in establishing and operating a buying group between competing firms in a compliant manner may outweigh the potential benefits of joint purchasing; and

(iv) The Revised Merger Guidelines suggest (at para. 4.24) that acceleration of a platform towards an inevitable tipping point may entail an SLC in respect of the interim period. For consistency, the Revised Merger Guidelines should also acknowledge that accelerating the realisation of consumer benefits through an

[40] This point is acknowledged at para. 5.21 of the Revised Merger Guidelines (in the context of dynamic competition) but is equally important in the context of assessing merger-specific efficiencies and entry prospects in other contexts.

[41] Indeed, the Revised Merger Guidelines anticipate such concerns in the context of discussing input foreclosure, at para. 7.14.

acquisition would generate efficiencies sooner than would have been possible under an organic strategy.

10.3 The acknowledgement that environmental benefits may constitute relevant customer benefits ("**RCBs**") for the purposes of section 30 of the Enterprise Act 2002 is welcome. In due course it would be helpful if the CMA could incorporate this acknowledgement into its guidance on *Exceptions to the duty to refer* (CMA64) (December 2018), and provide tailored guidance on how the CMA will apply the analytical framework described therein to environmental RCB claims. The evidence needed to show that environmental benefits are likely, and the timeframe in which they may be realised, is likely to be very different from the illustrative examples currently addressed in CMA64.

11. Market Definition

11.1 The over-arching message of the Revised Merger Guidelines on market definition is consistent with the 2010 Guidelines and the CMA's decisional practice: i.e. that market definition provides a useful analytical framework in which to consider the competitive effects of a merger, but it is a tool rather than an end in itself. We agree with this proposition, but would emphasise that the process of assessing and defining a relevant market imposes a degree of analytical rigour at the outset of the competitive assessment which will in many cases contribute to better and more robust analysis of a merger's effects. The Revised Guidelines should make clearer that in many cases the process of defining a relevant market will nevertheless remain a useful exercise, even if it only provides a starting point for a fuller competitive assessment.[42]

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[42] As the CMA notes, the statutory test for an SLC finding requires that the SLC arise "within any market or markets in the United Kingdom for goods or services" (sections 22(1)(b), 33(1)(b), 35(1)(b) and 36(1)(b) of the Enterprise Act 2002). Proceeding on the basis of a sound consideration of the potentially relevant market should therefore also help to ensure that the CMA's inquiry is geared towards meeting the statutory test.