ICLA UK Response to the CMA's consultation on its Merger Assessment Guidelines

1. **Introduction**

1.1. The In-House Competition Lawyers' Association UK ("ICLA UK") is an informal association of in-house competition lawyers in the UK comprising around 100 members. ICLA UK meets usually twice a year to discuss matters of common interest, as well as to share competition law knowledge. ICLA UK does not represent companies but rather is made up of individuals who are experts in competition law. As such this paper represents the views of the ICLA UK members and not the companies who employ them, and it does not necessarily represent the views of all its members.

1.2. ICLA UK is part of the wider In-house Competition Lawyers' Association of in-house competition lawyers across Europe and in South East Asia which currently numbers more than 450 members based in different countries around the globe.

1.3. Because of their role, in-house competition lawyers have a clear interest in a simple and straightforward competition law regime that prioritises legal certainty, minimises costs, and does not represent a disproportionate demand on businesses' time and resources.

1.4. ICLA UK is grateful for the opportunity to feedback on the CMA's proposed Merger Assessment Guidelines (the "Guidelines"). Guidelines in this area continue to be welcome and this is an opportunity to provide clarity for firms considering and/or involved in a relevant merger situation ("RMS") and their assessment of (i) whether it may result in a significant lessening of competition ("SLC") such that voluntary notification is advisable; (ii) the likelihood of a potential SLC impacting the scope of the merger, including potential divestments or other remedies; and (iii) if a potential SLC is significant such that it is likely to result in a prohibition which may then result in merger opportunity not being pursued.

1.5. Guidelines providing more certainty for business are particularly important in this area of UK competition law because the UK merger regime inherently causes more uncertainty as compared with other jurisdictions due to its various "outlier" features, including the voluntary notification regime, the use of a share of supply test, and the approach to material influence including the possibility of considering shareholdings of less than 15%.

1.6. ICLA UK's responses to the consultation are set out below.

2. **Consultation Question 2: Are the Draft Revised Guidelines sufficiently comprehensive? Do they have any significant omissions?**

2.1. The Guidelines focus particularly on harm rather than on benefits and efficiencies. For example, there is a list of situations in which mergers may generate an SLC, but no list of the types of mergers which may be less likely to generate an SLC. This one-way approach limits the usefulness of the Guidelines and may have harmful effects on business:

2.1.1. First, the weighting of the guidelines towards what is harmful, omitting acknowledgement of what may not be problematic, may have a chilling effect on M&A activity, to the detriment of the wider economy and thereby consumers. It would help

businesses if the CMA also generated a list of types of merger that are usually less likely to generate concerns.

2.1.2. Second, loose guidelines can also increase the risk of opportunistic actions by third parties that may waste CMA time and further undermine business certainty. One example of where loose guidelines may generate opportunistic actions is around the definition of material influence. While this is not a part of this consultation, there needs to be a clear line between what constitutes a merger situation and what constitutes an agreement between undertakings. South Africa has a material influence test in its merger control regulation. This has recently been subject to opportunistic actions by complainants in relation to agreements between competitors that do not involve any equity stake being taken. Complainants have alleged that agreements between competitors have enabled one party to exercise a degree of material influence over the other. There is potential for this to arise in the UK as well, and it would be helpful for the CMA to set out what is not material influence as well as what might be material influence, to create more business certainty.

2.1.3. Third, the characteristics of certain industries mean that this focus on harm, without appropriately balanced efficiencies, has a particularly high risk of negative impact. As an example, take industries with high fixed costs and low marginal costs (for example, telecoms). In such markets, high fixed costs mean that the market only supports a small number of players (all the way down to natural monopolies). Such markets may generate high margins as marginal costs are very low, while generating returns on capital that are below the cost of capital, particularly if fixed costs increase over time. Firms may not exit the market as they can still generate a return (even if it is below the cost of capital), but they may also be unable to invest in more efficient infrastructure, leading to significant losses in dynamic investment-based competition. Mergers in such oligopolistic markets may generate significant improvements in efficiency and lead to better outcomes for consumers. However, the generic CMA Guidelines puts such mergers at a disadvantage.

2.1.3.1. First, the suggestion that a four to three merger involving a market leader is an example of a problematic merger is included, without taking account how this will be contingent on the specific market context in which the merger is taking place. In high fixed cost markets, a four to three merger may be very positive for consumers, as it may unlock new investment without leading to an increase in prices. Setting out SLC examples in a generic manner that does not take account of the heterogeneous nature of markets does not assist with deal certainty. If it wishes to adopt this approach, the CMA should also consider setting out examples of mergers where an SLC is less likely to arise. Were it to do so, it would likely wish to identify a number of caveats to explain the circumstances in which such mergers could be problematic. In the same vein, in order to be more even handed, if the CMA wishes to set out examples of problematic mergers, it should highlight market contexts in which such mergers may not generate an SLC.

2.1.3.2. Second, the focus on margins when assessing horizontal unilateral effects (see paragraph 4.11(b)) discriminates against high fixed cost market sectors. A

common feature of such markets is that they can have high margins (in terms of EBITDA) but low profitability (in terms of returns on capital employed set against cost of capital - telecoms in general at present suffers from returns below the cost of capital). The Guidelines make no acknowledgement of this feature of high fixed cost markets.

2.2. The focus on harm and omission of an equivalent focus on benefits also impacts the usefulness and efficacy of the section on dynamic competition.

2.2.1. First, note that assessments of horizontal unilateral effects are prone to an analytical availability bias in favour of static effects. It is easier to conduct an upward pricing pressure analysis, which can produce a misleadingly precise output, than it is to assess future gains or losses in dynamic efficiency. It is also more straightforward to assess short term price effects than non-price effects, such as future investment, and investment efficiency. However, the more significant gains or losses to competition may arise from the dynamic effects.

2.2.2. Second, the section in the Guidelines on the loss of dynamic competition has no sub-section on the potential gains to dynamic competition that may arise from mergers. In high fixed cost industries where there is competition over investment, mergers may generate gains for dynamic competition, as they increase the capacity of individual firms to invest in new infrastructure that increases product quality and reduces costs. These types of consideration are treated as an afterthought in the guidance, in the section on "countervailing factors".

2.3. While the Guidelines take an expansive approach towards identifying what has the potential to generate an SLC, it takes a narrow approach to the identification of efficiencies that may outweigh an SLC. The CMA notes that to date in its experience it has been rare for proposed mergers to be cleared on the basis of efficiencies (paragraph 8.7). However, this may be due to the application by the CMA of an unduly restrictive analytical framework when assessing efficiencies as compared with theories of harm, rather than a lack of sufficient efficiencies. We would encourage the CMA to reflect on this and consider further a more balanced approach in the Guidelines.

3. **Consultation Question 3: Do you have any suggestions for additional or revised content that you would find helpful?**

3.1. In relation to evidence and how this assessed by the CMA, further clarity would be welcome.

3.2. First, as regards internal documents upon which the CMA has been placing greater importance and which the Guidelines state it will continue to do so in the future, the Guidelines make the following statements. ICLA UK has added its reactions immediately after each of these:

3.2.1. *Where internal documents support claims being made by merger firms or third parties that have an interest in the outcome of the CMA's investigation, the CMA may be likely to attach more evidentiary weight to such documents if they were generated prior to the*

period in which those firms were contemplating or aware of the merger, or if they are consistent with other evidence (paragraph 2.28(a)).

3.2.1.1. There are many different types of internal documents and internal documents are generated by many different people for many different reasons. It would be useful if the Guidelines could be more specific as to the types of internal documents that would be sufficient to constitute actual evidence of a firm's intent or at least set out those documents which the CMA recognises would not alone constitute sufficient evidence.

3.2.1.2. In particular, ICLA UK believes the context of a document and not just its content is relevant to determining whether it constitutes sufficient evidence. This ought to be recognised by the Guidelines and appropriate indications given. Failure to take into account context could have a harmful chilling impact on businesses brainstorming and debating options, and thereby on innovation. By context we refer, for example, to:

3.2.1.2.1. The author of a document – e.g. a junior or inexperienced colleague versus a senior colleague experienced in the subject of the document. Less weight, if any, should be placed on the former as the junior inexperienced colleague cannot and does not steer or represent the business and its commercial strategy. Further, junior colleagues may be more prone to exaggeration in situation where they are working hard to impress or convince more senior colleagues;

3.2.1.2.2. The purpose/type of a document – e.g. a no hands tied brainstorming exercise prior to seeking legal input versus a strategic business plan or board paper to be submitted to a senior management team for approval, or, a draft versus a final version of a board paper. Less weight, if any, should be placed on the former. To do so would stifle the ability of business to brainstorm and innovate, when brainstorming occurs prior to scenarios and ideas then being presented to legal departments for review and feasibility during which anti-competitive proposals are rejected not just by legal departments but by management; and

3.2.1.2.3. The timing of a document – e.g. a historical document prepared by employees who may no longer be in the team/company versus documents contemporaneous to, or in the period pre-dating (reasonably), the transaction. Less weight, if any, should be placed on the former where they should not be presumed to reflect the will or culture of current management, especially where such a change of approach is supported by evidence.

3.2.2. *The decision by a merger firm to enter or expand through a merger (ie inorganically) may supplant any efforts or plans the firm would otherwise have made towards organic entry or expansion. Therefore, when considering whether a merger firm may have entered or expanded absent the merger, the CMA may consider the incentives and ability of the firm*

to enter or expand and other available evidence. A lack of evidence of efforts or explicit entry or expansion plans made available to the CMA will not be sufficient to demonstrate that the firm would not have entered absent the merger (paragraph 2.28(c)).

3.2.2.1. Given that the Guidelines state that a lack of evidence, including internal documents, is not enough for the CMA to determine that organic entry or expansion is unlikely absent the merger, the Guidelines ought to provide more detail on what evidence, in such a scenario, the CMA would rely upon to find entry/expansion is in fact likely.

3.2.3. *An absence of internal documents pointing to, for example, competitive interactions between the merger firms may not be probative if the merger firms do not normally generate documents in the ordinary course of business or where merger firms have document retention policies whereby documents are regularly deleted* (paragraph 2.28(d)).

3.2.3.1. Given that the Guidelines state that an absence of internal documents may not be probative, the Guidelines ought to provide more detail on what evidence, in such a scenario, the CMA would rely upon to find in fact e.g. competitive interactions.

4. **Consultation Question 4: Do you agree with the approaches set out in the Draft Revised Guidelines?**

The large amount of CMA discretion causes uncertainty for business and may have a chilling effect on pro-consumer market transformation

4.1. The Guidelines grant the CMA a great deal of discretion and room to use its judgment in many areas. We understand that the CMA does not wish to limit its options or tie its hands in any way, however the Guidelines as currently drafted raise a number of concerns:

4.1.1. The amount of discretion left to the CMA creates greater uncertainty which, combined with the UK merger regime's outlier factors mentioned in the introduction, may have a chilling effect on pro-consumer transactional activity in the UK.

4.1.2. This wide scope for discretion creates the risk of inconsistency in merger assessment between one CMA decision and the next and even between different CMA case teams. Again this creates more uncertainty, which in turn tends to have a chilling effect on business strategy involving transactions.

4.1.3. The Guidelines ought, in ICLA UK's view, to create more certainty not less. The Guidelines clearly state in paragraph 1.12 that the review of each merger is case-specific, the Guidelines are just a framework which will be applied flexibly and that the CMA may depart from the Guidelines where appropriate. These caveats mean that whatever the content of the Guidelines, the CMA is protected from its options being limited in any way. Consequently, the Guidelines themselves should provide more specificity and examples and leave less to CMA discretion and judgement, given that CMA discretion may be exercised in any event. Without such a change the Guidelines are much more

limited in their usefulness to firms and indeed could have an anti-consumer chilling effect on business transformation and market evolution.

4.1.4. Specific examples of this overly broad discretion include (though are not limited to):

4.1.4.1. In paragraph 5.12 of the Guidelines regarding loss of future competition, which refers to the CMA concluding on the prospect that one of the merger firms would have entered absent the merger, without concluding on the precise characteristics of the product it would launch, or which particular assets (out of a set of possible options) it might acquire in order to enter. If the CMA is unable to conclude on these elements it must be because the firm itself had not concluded on these factors such that entry is uncertain. However as drafted the Guidelines would allow the CMA, which lacks relevant industry-specific experience and expertise, to replace the view of a firm's management in deciding whether or not such a firm would enter with its own judgment. This is too wide a discretion and any such conclusion ought to be based on material evidence, not the CMA's judgment.

4.1.4.2. In paragraph 5.21 of the Guidelines regarding loss of dynamic competition, the CMA states it may conclude on the prospect that one of the merger firms would have entered absent the merger, without concluding on the precise characteristics of the product it would launch, or which particular assets (out of a set of possible options) it might acquire in order to enter. In making such a conclusion the CMA will consider a broader pattern of dynamic competition in which the specific overlaps may not be identified easily at the point in time of the CMA's assessment. Again, this leaves a great deal of discretion to the CMA and the making of such impactful conclusions ought to be made on firmer evidence than "broader patterns".

4.1.4.3. Market definition in Section 9. Whilst we agree that a highly specific description of any particular market definition is not always necessary, it should not be forgotten that market definition, whether taking a simple or complex approach, should be based on objective evidence and not the CMA's subjective views. For example, paragraph 9.3 suggests that the CMA may calculate concentration measures on multiple different bases, including and excluding different firms, "depending on which firms the CMA wishes to compare". The inclusion of firms in any calcautions of concentration ought not to be based on which firms the CMA wishes to include or not, but rather on which firms constitute a competitive constraint based on objective evidence. Further, the CMA should not forget its obligations pursuant to the Enterprise Act to identify the market or markets within which an SLC exists (Sections 22 and 35 of the Act for completed mergers and sections 33 and 36 of the Act for anticipated mergers) in respect of which *British Telecommunications PLC v Office of Communications* [2017] CAT 25 (BCMR) Paragraph 156 acknowledges that only in "certain situations" (not most or all) it may be possible for an authority to avoid conducting a full relevant market analysis.