Microsoft's Response: Competition and Markets Authority's Call for Information on Phase 2 merger investigations

25 August 2023

Executive Summary

Microsoft welcomes the opportunity to respond to this Call for Information (CFI). Now is an important time to reflect on the Competition and Markets Authority's (CMA) approach in conducting Phase 2 merger reviews, especially when its processes and merger assessment principles are being applied in the context of innovative and highly dynamic markets.

Microsoft fully supports the CMA's aim to optimise how these investigations are run. Having recently undergone a detailed review of the proposed acquisition of Activision Blizzard King (ABK), we highlight below several recommendations for consideration by the CMA.

Given the terms of the CFI, these recommendations are intended as suggested enhancements within the existing statutory structure based on Inquiry Groups and case-teams.

The focus on Recommendations 1 – 3 in Part A below is on maximising effective and transparent engagement with the Inquiry Group and case team to improve processes covered by the CFI, including especially timely engagement on and development of remedies.

Recommendations 4 and 5, set out in Part B, cover ways in which we consider the robustness of decisions can be improved. Recommendation 6, in a short Section C, describes how a more targeted approach to information gathering could result in the CMA's and the parties' resources being used more effectively. Annex 1 provides suggested revisions to the existing timetable and structure for engagement to best deliver on these Recommendations.

In summary, the headline points in the Recommendations are:

1. Merging parties should be able to interact directly with their Inquiry Group on substantive issues earlier in Phase 2. This would assist the Group to stress-test the theories of harm identified by the CMA at Phase 1 more quickly and provide the main parties with early visibility of the case against them. The focus can then turn to developing effective responses or solutions in a timely fashion.

2. The Inquiry Group should be empowered and encouraged to engage with the merging parties on remedies at any point during the process, with sufficient ability to adapt to find effective solutions tailored to the facts in each case. Flexibility on timing and the substance of the remedy type is particularly important for effective coordination in global deals (to enable early CMA discussions in parallel with other jurisdictions).

3. Ongoing ad hoc engagement between the parties and both the case team and the Inquiry Group should be encouraged. This will help address issues quickly.

4. The main parties should have earlier effective access to key materials and evidence, both exculpatory and adverse (including third party submissions and analysis subject to

appropriate confidentiality protections). Not only is this pivotal to robust decision-making, but such type of disclosure, coupled with the right to be heard in other Recommendations, are essential elements of procedural fairness and due process. Furthermore, given the judicial review appeals standard, the CMA investigation is the only opportunity for facts to be stress-tested – this makes access to documents, at appropriate stages of the Phase 2 process, vital.

5. Implementing existing and well-understood mechanisms for quality assurance in regulatory decision-making can ensure the Group's conclusions are more robust. Formalising internal scrutiny, especially on expert topics such as economic models, is one way of putting such mechanisms into effect.

6. Data and input gathering should be more targeted and tailored to enhance efficiency. Ongoing ad hoc engagement (Recommendation 3) would also facilitate this.

The remainder of this document sets out more detail on each of these Recommendations. We look forward to continuing to engage with the CMA on this important topic as its considerations on how to enhance the regime develop over the coming months.

A. Engagement with the Inquiry Group and case team

1. Earlier substantive interaction with the Inquiry Group

The merging parties should have an opportunity to directly engage with their Inquiry Group at the start of the merger review. Currently, the parties' first opportunity to meet the Group is not until week 4 or 5, which is quite late down the line, a sixth of the way through the full 24-week timeline. Even at that stage, the focus at the Site Visit is on a 'teach-in' on the parties' products and services rather than the substantive issues the Inquiry Group is required to consider.

UK merger control tends to be the "long pole", the project with the longest completion date, in multi-jurisdictional filings. Frontloading key aspects of the substantive discussion would allow for the following opportunities:

a. **Inquiry Groups can more quickly develop their position on relevant theories of harm** through direct interaction on technical and factual matters with the parties and by stress-testing the theories of harm, developed by the CMA at Phase 1, together with the underlying evidence;

b. **more frequent and intense remedies discussions can also begin earlier** (if needed) than under the current process, with more time to develop solutions to address each Group's specific concerns (and, where relevant, in parallel with other reviewing jurisdictions).

   Note that this is also dependent on a move towards flexibility in the CMA's broader policy on remedies, including a more fluid view on the current distinction between structural and behavioural remedies.

Microsoft also considers that the format of the Main Party Hearing should be restructured to encourage a more discussion-style dialogue on key topics, enabling a more substantive exchange at this crucial point in the assessment – before the Provisional Findings (PFs) are issued. The current predominantly interrogative "question and answer" format means that there is little opportunity for substantive engagement on the theories of harm.

Annex 1 describes how we envisage the revised timetable could work in practice, especially in the early part of Phase 2, as compared to the current process.

2. A greater focus should be placed on finding solutions

In response to the CFI, the proposals below provide ideas on how to make without prejudice remedies discussions work more successfully. Along with Recommendation 4, focused on early access to key evidence, and Recommendation 5 on the enhancement of CMA processes of internal challenge, they can also improve the likelihood of any errors being corrected. As a result, the focus of engagement can turn to solutions quicker.

Early remedies discussions

Microsoft considers that Inquiry Groups, as well as key members of the case team and the Remedies, Business and Financial Analysis (RBFA) Group should be given greater flexibility to hold early discussions with the merging parties on potential remedies. These discussions would be on a without prejudice basis and, crucially, the CMA should be more open to *providing feedback* on remedies being proposed and considering iterations of these throughout the process.

Remedy design is often highly complex. Despite this, currently the timetable during which workable solutions can be found is unnecessarily compressed as detailed remedies conversations do not often begin until well after PFs. Starting remedies conversations earlier means that:

a. **there is an opportunity for a more constructive and iterative process** that allows for issues to be resolved more efficiently. The nature and scope of remedy proposals can be adjusted in this way as the Group's own thinking is refined through nuanced and constructive engagement.

   Combined with a more transparent process on all the key **evidence obtained by the CMA** (see below), the parties can understand and begin to respond to the case against the merger quicker. This would allow more time to be focused on correcting errors/misunderstandings and finding solutions, which is indispensable for a successful remedy "design-and-offer" dynamic.

b. **the Group, the RBFA and the parties are likely to be more engaged in seeking to craft workable solutions, especially if there is an ongoing and clear feedback loop**. Encouraging an open dialogue and allowing for more time enables each of these three groups to better understand each other's position as well as the views of complainants, where they have valid concerns. The ultimate result is

that the remedies formally put forward by the parties are more likely to meet the desired outcome of specifically addressing the Group's theories of harm.

Making the regime generally more flexible would also encourage a more pragmatic approach to behavioural remedies, as described immediately below.

c. **the CMA's own coordination with counterpart regulators on global transactions is facilitated** (see further below)

Flexibility in approach when developing proportionate remedies

Microsoft recommends that, in cases involving novel theories of harm (particularly in nascent markets), the CMA also be open to discussing remedies that might not have previously been considered or accepted. Clearly, an assessment of dynamic markets cannot be limited to static solutions and a rigid distinction by remedy-type (i.e., behavioural and structural) is unhelpful.

Microsoft suggests that the CMA specifically consider revising the CMA Remedies Guidance to take these points into account, along with the broader procedural points in this paper.

An updated approach would also be more consistent with measures that the Digital Markets Unit (DMU) is expected to impose in the medium term. The Codes of Conduct that will be developed for firms with Significant Market Status are likely to cover a range of different commitment types, but most (if not all) are expected to be behavioural in nature. Applying a blanket prohibition on behavioural remedies in digital markets for merger cases therefore appears to be an inconsistent policy choice. For example, in digital content markets, where the vast majority of content is in-licensed from third parties, it is entirely reasonable to conclude that licences can be appropriate remedies (subject to the scope, duration and restrictiveness of the necessary licences).

Finally, while monitoring of behavioural remedies has historically been a concern, the DMU will be provided with enforcement powers as sector regulator for the digital market under the upcoming Digital Markets Consumer and Competition bill. The monitoring and revision of behavioural remedies – both under the merger and regulatory regimes – can be resolved in this way, much as it is the case with other regulated markets, such as telecoms.

Importance of the international element

The CMA has frequently acknowledged the importance of international coordination, especially when counterparts are reviewing the same global transaction. Microsoft recommends that the CMA continue to actively take into account the status of ongoing reviews of deals in other jurisdictions, especially in deciding when to begin engagement on remedies. Recent divergence between decisions by the CMA and European Commission (EC), for example in Cargotec/ Konecranes, were at least in part, a result of timing issues capable of being addressed through more flexibility.

Particularly in the context of global digital transactions, the CMA must be cognisant of the fact that its decisions on remedies may have significant extra-territorial effects. While the CMA will rightly focus on the impact of the transaction on UK consumers, it should give appropriate

consideration and weight to any remedies likely to be implemented in countries outside the UK, so that its approach to these is both proportionate and properly reflects their impact and effectiveness across jurisdictions.

3. Ad hoc engagement can help to resolve specific issues between formal meetings

Both the case team and the Inquiry Group should have ad hoc ongoing engagement with the parties and their advisers. This is especially the case if such discussions can resolve important areas of uncertainty quickly. Having the Inquiry Group present at these sorts of meetings will provide them with the opportunity to raise questions with the parties on a more ad hoc basis than is currently possible. It will also provide the parties greater confidence in the process through allowing more direct interaction with the decision-makers.

Areas for discussion could include explanations and questions on:

- the evidence or further submissions that might be required to confirm specific points the Group is considering;
- the data or evidence from the main parties that would clarify or determine the credibility of new or evolving issues or theories of harm (particularly those raised by third parties);
- areas dealing with economic analysis; and
- meetings to explore the meaning and relevance of certain internal documents of the merging parties.

Ad hoc meetings can be conducted with only some members of the Inquiry Group being present, if needed.

B. Ensuring decisions are robust

4. Protecting parties' rights of defence and access to evidence

Early appropriate engagement and disclosure

To ensure CMA processes and procedures are reasonable and fair, the main parties should be provided fuller transparency, i.e. timely and useful information, throughout the entire Phase 2 review (in line with the 2010 OFT Market Studies Guidance, for example).

Recommendations 1 – 3 above seek to enhance appropriate early transparency on the Inquiry Group's thinking and ensure that the merging parties are given sufficient opportunities to meaningfully assess the evidence being used against the transaction and to respond and be heard through improved engagement.

In addition, it is important that the Phase 2 process allows the evidence obtained, and relied upon, by the CMA to be stress-tested properly. Indeed, in an environment where mergers are subject to a judicial review appeal standard, the Phase 2 process is the only opportunity for the facts and evidence relied upon by the CMA to be properly assessed and balanced against all available evidence.

Two specific areas that require additional disclosure of evidence to the parties are:

(i) all the documents and data analysis on which the Inquiry Group is considering relying upon in the PFs and the Final Decision;
(ii) receiving the fullest possible version of third parties' submissions and any supporting documents or other material.

This disclosure needs to take place at a sufficiently early stage in the process so that the parties can assess it and make representations. These could be both on evidence the Group is proposing to rely upon, but also exculpatory evidence on the CMA's file, before the Group reaches its provisional findings, making the overall process more efficient. The obvious helpful outcome for all stakeholders is that decisions are likely to be more robust, reversals after PFs are less likely, and the potential for appeals will be reduced.

Microsoft proposes that disclosure take place at (at least) three separate stages:

(i) shortly after the opening of the Phase 2 process, the parties should be provided with access to the evidence obtained by the CMA during Phase 1;
(ii) alongside the Working Papers, access should be provided to any evidence obtained by the CMA up to that point in Phase 2; and
(iii) alongside publication of the PFs, access should be provided to any further evidence obtained by the CMA.

Earlier and improved access to key materials would also enable effective remedies to be considered and even submitted *before* the Main Party Hearing, thereby enabling potential solutions to be constructively discussed at that forum (crucially, in advance of PFs).

Finally, enhancing transparency may well also assist in limiting the potential for divergent outcomes with other jurisdictions. For example, apart from our experience as part of the ABK merger inquiry, divergent approaches by the CMA and EC (which almost always consider very similar market conditions) have been seen in Facebook (Meta)/Kustomer, Amazon/iRobot, Booking/Etraveli, S&P/HIS Markit and Cargotec/Konecranes.

Stress testing third party submissions

It is, of course, entirely appropriate that the views of third parties are sought and carefully considered by Inquiry Groups. The impact of a transaction on customers (and suppliers) is clearly of real import and relevance. Similarly, competitors can be a material source of views and data, subject to the obvious caveat about self-interest. That said, it is important for the integrity of the Group's assessments that complainants (and their submissions) are subject to the same style of approach and evidentiary standards as the main parties.

While third parties may not have access to details about the transaction or the main parties' activities, where they make substantive submissions and/or claims that may need to be justified, the CMA can:

(i) provide non-confidential versions of complainants' submissions, requesting a reasoned and evidenced response to the claims; and/or
(ii) establish a confidentiality ring where such information is shared at least with the parties' advisers.

In addition, the CMA can use questionnaires to gather necessary data from the main parties to cross-check the position. A bolder, more constructive approach by the case team to challenge potentially baseless confidentiality claims by complainants would also help to deliver necessary disclosure to the merging parties, and so avoid third parties preventing proper scrutiny of their claims.

Further, Microsoft recommends that the CMA request that complainants provide contemporaneous documents evidencing their claims concerning the conduct and incentives of the main parties.

A combination of these approaches, all of which are currently within the CMA's existing powers, are being used by a number of other competition authorities, including the EC, the Australian Competition and Consumer Commission, the New Zealand Commerce Commission and the Brazilian CADE, to successfully stress-test complainants' views. For example, the EC provides full access to the file and checks complainants' positions through questionnaires (to the parties and the market more broadly) in order to collect the most relevant evidence.

5. CMA internal processes should be enhanced

Microsoft recommends that the CMA should consider institutionalising a process of internal challenge to Inquiry Groups. Such peer review level of scrutiny should be led at the Executive or Senior level (e.g., one or more of the Executive Director or Senior Directors of Mergers, the General Counsel or the Chief Economist). The purpose is to provide a "red team" (or "devil's advocate") evaluation on the competition assessment and supporting evidence base, especially where speculative theories of harm are being considered, and to stress test thinking on the suitability and sufficiency of remedies proposed. The most suitable time for this type of review/s would need to be identified, at least once during Phase 2, possibly before PFs.

The limited nature of judicial review of decisions means that such internal processes do not only ensure the robustness of hugely impactful decisions, but are also one of the very few ways to challenge decision-making groups.

It is worth noting that internal quality assurance checks, designed to protect the parties' rights to a fair process, already exist for Phase 1. The appointment of both a devil's advocate and a senior CMA member, outside the case team, as decision-maker are good examples.

Similar processes for internal challenge have also been standard practice, especially for strategic decisions, for authorities like Ofcom and various Government Departments, in compliance with recommendations in the 2013 Macpherson Review.

C. Maximising use of CMA resources

6. Targeted data and input gathering

Microsoft recommends that the financial and market questionnaires sent at the opening of Phase 2 reviews be more narrowly targeted at the information that is actually required to test which theories of harm can be considered most credible by the Group. This may require

sending staggered questionnaires, with certain areas held back until the Main Party Hearings. If the specific questions remain live after the Main Party Hearings, requesting the material through supplementary formal requests, informed by the evidence already gathered by the CMA, remains an option.

More agile use of questionnaires would enable more fluid and pragmatic engagement with the main parties. Resources are most efficiently deployed through interaction on the Group's actual concerns, particularly where these relate to potential competition in nascent and/or rapidly evolving markets (or where there are more speculative theories of harm).

As noted above on ad hoc engagement, Phase 2 Project Managers should also routinely maintain an informal open channel of communication with the external advisors. Such constructive discussions can only streamline reviews, enhance cooperation, and more generally drive efficiency in investigations.

Annex 1: Proposed adjusted Phase 2 timetable

The adjusted process in this Annex describes how the stages of merger review, especially before Provisional Findings (PFs) are issued, could be adjusted to implement the Recommendations in Microsoft's submission.

<table>
<tr><th>Current process</th><th>Timing</th><th>Adjusted process</th><th>Timing</th></tr>
<tr><td>REFERENCE DECISION</td><td>Day 1 of Phase 2</td><td>REFERENCE DECISION</td><td>Day 1 of Phase 2</td></tr>
<tr><td></td><td></td><td>Access for main parties to key internal materials and 3rd party evidence obtained by CMA during Phase 1</td><td>Weeks 1 to 2</td></tr>
<tr><td rowspan="2">RFIs collecting relevant evidence on all possible areas</td><td rowspan="2">Weeks 1 to 6</td><td>SITE VISIT
Microsoft recommends that site visits, devoted mainly to fact-finding and discussion of relevant technical matters, be conducted at the start of Phase 2. This type of open discussion, essentially a teach-in, would enable all key CMA staff, especially the Inquiry Group, to fully understand the relevant products/services as well as the technical abilities and constraints of the parties and their competitors. It would also enable the CMA to benefit and engage fully with technical and other experts, fielded by the parties, thereby reducing the overall time and lift needed for them to get up to speed.

If the CMA considers it would be useful, the parties could make opening statements to help set the direction of the review.</td><td>Weeks 1 to 3</td></tr>
<tr><td rowspan="2">High level RFIs to assess which markets could present realistic competition concerns – proposal is to collect evidence across all relevant areas, but not in as much depth as that required in existing RFIs</td><td rowspan="2">Weeks 1 to 6</td></tr>
<tr><td>SITE VISIT</td><td>Week 4</td></tr>
<tr><td colspan="2"></td><td>ISSUES MEETING
Meeting to specifically discuss key aspects of the competition assessment before the Issues Statement is finalised. This would enable an open and transparent consideration of any theories of harm being explored by the Inquiry Group and the evidence required, especially for the competition assessment.</td><td>Weeks 4 to 5</td></tr>
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ISSUES STATEMENT	Weeks 4 to 5	ISSUES STATEMENT	Weeks 6 to 8
		Access for main parties to key internal materials and 3rd party evidence obtained by CMA since commencement of Phase 2 investigation	*Weeks 6 to 9*
		Plus targeted RFIs (requiring the same level of detail as current RFIs in week 1) to collect evidence on specific areas that present realistic competition concerns outlined in the Issues Statement. --- The Issues Statement can be produced at about the same time as it is today, but the earlier opportunity for the Inquiry Group to engage directly with the parties, means that they can express a more developed position of their own, having stress-tested the theories of harm developed at Phase 1. It is also important that the Group's position would take into account matters covered during the site visit and the Issues Meeting, along with key internal documents and third-party evidence. Importantly, the parties' rights of defence are better protected by providing them access to key internal materials and third-party evidence on which the Issues Statement is based. At this stage, the Inquiry Group can also identify – either formally through the Issues Statement itself or (preferably) informally through ad hoc discussions – what further points and evidence it needs to confirm before delivering the annotated Issues Statement/Working Papers.	**Weeks 6 to 8** **Ongoing from w6**, after Issues Statement
		Contemporaneous and ongoing w/out prejudice remedies discussions until Final Decision, if needed (see also entry on p. 4 below)	Ongoing from w6

Responses to Issues Statement	Weeks 6 to 7	**Responses to Issues Statement** Just as an Issues Statement will be a more robust document, informed by additional interactions and material, so would the main parties' response. The parties would be able to address the more developed thinking by the Group with more developed and detailed responses of their own, before the Group crystallises its thinking in the PFs. The importance of this point is also made clear by the fact that there is only a very limited number of instances where Final Decisions came to conclusions that differed from the PFs, including Amazon/Deliveroo, NortonLifeLock/Avast and Copart / Hills Motor. Given the current limited standard of review before the CAT, this and the stage just after the PFs are the only opportunities for consideration and assessment of the facts.	Weeks 8 to 9
Annotated Issues Statement / Working Papers	Weeks 11 to 13	**Annotated Issues Statement and Working Papers**, taking into response to Issues Statement and evidence from targeted RFIs	Weeks 8 to 10
MAIN PARTY HEARING	**Weeks 11 to 12**	**MAIN PARTY HEARING** To ensure procedural fairness and avoid enshrining confirmation bias, this hearing would need to take *place* before the PFs are published. It should allow the parties to respond to the full case against the merger, including the supporting evidence, in front of the decision-makers. Under the current regime, it is the second chance for in-person engagement with the Group. Apart from implementing the additional early-stage interactions above, the CMA should re-consider the type of engagement and scheduling / topic areas to cover.	**Weeks 8 to 10**

		A more discussion-style dialogue on key topics enable a more substantive exchange at this crucial point in the assessment – before the PFs are issued. The current predominantly interrogative "question and answer" format means that there is little opportunity for substantive engagement on the theories of harm, which is largely done through the main parties' brief opening and closing statements. At this stage, the parties would also have the opportunity to respond to the Issues Statement, address adverse evidence from the file and discuss initial findings on the economic assessment and what else might be useful; and meaningfully engage on remedies (if they wish). If earlier ad hoc interactions can confirm the position on relevant, but often time-consuming areas, this could also be helpful to free up the schedule. For example, if comments in internal documents can be explored in some detail beforehand, only key points need confirmation on the day.	
PROVISIONAL FINDINGS	**Weeks 13 to 14**	**PROVISIONAL FINDINGS**	**Weeks 12 to 13**
		Access for main parties to key internal materials and 3rd party evidence obtained between Issues Statement and PFs	*Weeks 12 to 13*
		Contemporaneous and ongoing w/out prejudice remedies discussions can begin earlier but are likely to become more frequent after PFs	Ongoing from w6
Responses to PFs	Weeks 16 to 18	Responses to PFs	Weeks 14 to 16
RESPONSE HEARING	**Weeks 16 to 17**	**RESPONSE HEARING**	**Weeks 16 to 17**
Final Responses	Weeks 20 to 21	Final Responses	Weeks 20 to 22
FINAL DECISION*	**Week 24**	**FINAL DECISION***	**Week 24**

Written submissions
Face to face/hybrid meetings

* Possibility of extensions throughout, if needed