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8TH GLOBAL MERGER CONTROL CONFERENCE #1 The ECJ *Three/O2* Ruling: Everything Changed?

Webinar – 2 December 2020*

First webinar of the 8th Global Merger Control Conference organised in partnership with Dechert and Frontier Economics.

Laurence Bary

Laurence Bary set the stage for the *Three/O2* judgement (Case T-399/16), which was issued by the General Court in May this year. In that judgement, the General Court annulled the Commission's decision prohibiting a four-to-three merger in the telecom sector between O2 and Three in the UK (Decision COMP/M.7612). The Commission blocked the deal based on the significant impediment to effective competition test (the "SIEC test").

It considered that although the new entity would only hold approximately 40% of the market, the transaction would still remove an important competitive force (Three). The annulment has been presented by many as a landmark case for two main reasons.

> **"THE SIEC TEST WAS INTRODUCED IN 2004 BY THE NEW EUROPEAN MERGER CONTROL REGULATION ("EUMR") AND ALLOWS THE COMMISSION TO TACKLE THE SO-CALLED "GAP CASES"."**
> LAURENCE BARY

First, it is the first time that the General Court has ruled on the SIEC test and the standard of proof it requires. The SIEC test was introduced in 2004 by the new European Merger Control Regulation ("EUMR") and allows the Commission to tackle the so-called "gap cases", that is to say, mergers that do not create or reinforce a dominant position but still can harm competition.

Second, there has been a sharp increase in prohibition decisions in recent years. Since 2016, the Commission has blocked no less than six mergers, which is as much as the total number of mergers that were blocked between en entry into force of the EUMR in 2004 and 2015. In that context, the judgment may appear as a significant setback for the Commission's policy, and especially for the trend Commissioner Vestager has set.

David Foster

David Foster recalled that the merger brought together the number two of the market with the number four. Hutchison was not only number four but also a late entrant on the market and struggled to get itself a sustainable and profitable position. For that reason, even though O2 was large, the combination did not amount to single dominance. This was, therefore, a classic "gap" case because the Commission did not find either single or collective dominance. It is a case of quite wide applicability, and not just within the telecommunications sector: mobile mergers combine elements of both a classic retail merger together with a network infrastructure merger. The judgment, therefore, touches on many of the most important concepts in the Horizontal Merger Guidelines. Three points are particularly important.

"IN PARTICULAR, COMPETITIVE REACTIONS AND MERGER EFFICIENCIES ARE LIKELY TO HAVE AN OFFSETTING EFFECT. THIS POINT HAS RAISED CONTROVERSY."
DAVID FOSTER

First, the Commission has up to now given a wide interpretation of what is meant by an important competitive force. The Court has established that the concept was being used very widely and ruled that to be an important competitive force, an undertaking must be particularly aggressive, not only in terms of its competitive actions but also in the sense that it has to force others to respond. It is not enough to identify that a company is competing on the market, other players have to care sufficiently about its behaviour.

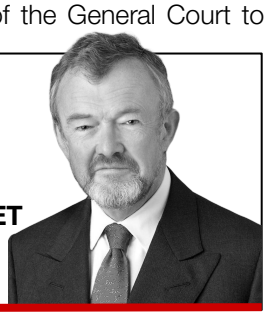
Second, as regards closeness in competition, the Court has provided details on what evidence is needed for an effect on competition to be regarded as "significant". More precisely, the Court notes that in an oligopoly market all players are close to a greater or lesser extent, and so the Commission must have evidence that merging parties are particularly close.

Third, the Court looked at upward pricing pressure ("UPP") analysis, an economic tool which has become increasingly common in merger assessments. The judgment holds that the UPP analysis as it stands in the Decision is not probative. The Court finds that these tests only look at the short-run effects that increase prices, and do not take into account any medium-term effects that bring prices back down again. In particular, competitive reactions and merger efficiencies are likely to have an offsetting effect. This point has raised controversy. The judgment says that there are two kinds of efficiencies: formal efficiencies (in the sense of Section VII of the horizontal merger guidelines) on the one hand and "standard efficiencies" on the other hand that arise in general from mergers and which should be reflected in the UPP analysis.

Ian Forrester

Ian Forrester believes that the judgement has not altered the classical presumption that four-to-three telecom mergers are examined very sceptically. Judicial review is narrow and technical. Judges produce a text which is agreed upon, elaborated sometimes between three, five or fifteen judges. It is very rare for a judgement of the General Court to turn the world upside down. Decisions from the European Commission are desperately long (this one has about 1000 pages) and there is a tendency to produce judgements of excessive length. That does not make them wrong, but it makes them rather heavy. Essential principles are not always easy to identify in these judgments.

"THIS IS THE BIG WEAKNESS OF THE ADMINISTRATIVE SYSTEM OF MERGER CONTROL. INDEED, EVEN IF THE MERGER WOULD HAVE BEEN PERFECTLY PRO-COMPETITIVE, IT WILL BE TOO LATE TO LET IT PROCEED."
IAN FORRESTER



To that respect, several points deserved to be shed some light on. One competitor was going to disappear after the transaction, and the Commission stated that even though Three was small, it was important on the market.The Court held that this was not enough to meet the SIEC test.

In another example, the Decision affirms that Three was a relatively close competitor to O2, but the Court holds that all competitors are by definition close, so the proper consideration to be made is whether Three was a particularly close competitor to O2.

The decision to merge was made very long ago and the appeal before the ECJ will not come before the end of next year. As a result, the merger is no longer achievable. This is the big weakness of the administrative system of merger control. Indeed, even if the merger would have been perfectly pro-competitive, it will be too late to let it proceed. This may be a serious issue for the EU competition system. One may wonder whether interim measures or greater importance of the Hearing Officer could remedy this situation.

Finally, it is possible to ask whether the Commission would be able to reach the same conclusion if it had to perform this analysis again. In any case, whether it loses or wins the case, the Commission will have it in mind for future transactions.

Gabriel Lluch

Gabriel Lluch explained that he does not expect a big change in the analysis of the Commission. The Commissioner in charge of competition, Margrethe Vestager, insists on the fact that there is no magic number for mobile network operators and that the Commission follows a case-by-case approach based on the own merits of each case. However, in practice, things are probably different, and it seems that the Commission tends to favour market outcomes that result in at least four players in that sector. In Austria (Case COMP/M.6497), Ireland (Case COMP/M.6992) and Germany (Case COMP/M.7018), the Commission considered that the reduction of the number of competitors in the mobile market would lead to higher prices and reduction of competition. All mergers were approved but subject to structural remedies.

"IT IS UNSURE WHETHER THE COMMISSION WILL ADAPT ITS ADMINISTRATIVE PRACTICE SINCE IT HAS CONSIDERED THE RULING TO BE CONTRARY TO THE SPIRIT OF THE EUMR."
GABRIEL LLUCH

The Commission ordered divestitures to create another competitor able to replace the competitive pressure lost through the transaction. However, it seems that remedies should be more flexible and adapted to each case. It may not make sense to require operators in all cases to divest their activities to create a new competitor.

The judgment of the General Court changed the model. However, further changes in the analysis should be reflected in future decisions and judgments to take into account the new conditions in the telecoms market. Indeed, traditional actors are being heavily challenged by large digital actors. This new innovative competitive pressure should be reflected during the merger review of the European Commission.

The Commission approach of four-to-three mergers seems to be troublesome. If followed, the reasoning of the Commission would mean that any four-to-three merger would automatically be problematic. This is not possible. On a market with a limited number of competitors, any reduction of competition can theoretically be considered as important. In the same way, any competitor can be considered to be a close competitor for another one. However, this approach cannot be acceptable since not every reduction of competition would meet the SIEC test and not every competitor may be labelled as a close one. Furthermore, there should be a high standard of proof when a horizontal merger does not raise dominance. The Commission should have to demonstrate that impediment of competition is the most likely outcome.

Finally, it is unsure whether the Commission will adapt its administrative practice since it has considered the ruling to be contrary to the spirit of the EUMR and has appealed the judgement before the Court of Justice. Furthermore, the Commission considers it important to maintain flexibility to conduct a case-by-case assessment of four-to-three mergers. In any case, companies and their counsels may hope that this judgment will lead the Commission to have a more flexible dialogue with the parties during the merger control proceedings. Otherwise, there is a risk of systematic judicial review, which is the worst scenario for companies and even for the Commission.

Gabriella Muscolo

Gabriella Muscolo provided her perspective on the *Hutchison/3G* case, which involved respectively the third and fourth-largest operators in the Italian retail mobile telecommunications market. According to the Commission, coordination would have been possible mainly due to the existence of sufficient market transparency and the presence of credible deterrence mechanisms. However, in Italy, the merged entity would have not resulted to be the clear market leader in retail mobile services (as in the *Three/O2* case), but the transaction would have led only to symmetric market structure; nor the Italian merger was related to undertakings that were having the same levels of UK ones in term capacity to innovate in the market and to steer market trends.

"THE 2004 EUMR THAT ADOPTED THE SIEC TEST HAS CREATED A DISCREPANCY WITH THE ITALIAN MERGER CONTROL SYSTEM, WHICH STILL RELIES ON A DOMINANCE TEST."
GABRIELLA MUSCOLO

As to the question on the cooperation between National Competition Authorities ("NCAs") and the Commission, in this case, the Italian Competition Authority ("AGCM") has been actively involved. For instance, the AGCM has examined very closely the whole set of commitments proposed by the parties. In particular, the AGCM considered that, in principle, the so-called "market mobile operator ("MNO") commitment" represented a valid solution to the Commission's concerns. The AGCM also identified some shortcomings which needed to be addressed. More in general, as regards NCAs participations in these cases, each telecom merger case was assessed on its own merits taking into account the specific market seizures, which varied from case to case. At the same time, the growing participation of NCAs in the merger review procedure has allowed the Commission to take advantage of their expertise *vis-à-vis* the peculiarities of national and oligopolistic markets, such as the mobile telecommunications ones.

Finally, the impact of the *Three/O2* judgement on the AGCM administrative practice may well be very limited. Indeed, although the analysis of mergers is similar, the Italian legal test is different from the European one. The 2004 EUMR that adopted the SIEC test has created a discrepancy with the Italian merger control system, which still relies on a dominance test; in Italy, to issue a veto decision, it must also be demonstrated that such a position can significantly and sustainably impede effective competition, worsening supply conditions on the relevant market.