

INTERNATIONAL COMPETITION NETWORK

FIRST ANNUAL CONFERENCE

NAPOLI, SEPTEMBER 28-29, 2002

ANALYTICAL FRAMEWORK OF MERGER REVIEW

Substantial lessening of competition/creation or strengthening of competition

**Comments of Richard Whish,
Professor of Law, King's College London**

- **My presentation today concerns the question of whether the dominance test contained in Article 2 of the EC Merger Regulation (the 'ECMR') or the substantial lessening of competition standard ('SLC') adopted in numerous jurisdictions is preferable for the control of mergers. I gave a speech on this, given at a seminar hosted by the Greek Competition Authority in Athens in April this year, in which I set out various arguments in favour of each standard. I concluded that, on balance, I favoured the SLC test, while recognising that the arguments are fairly evenly balanced. I do not intend to go over all those arguments again today.**
- **Nor do I intend today to discuss the 'politics' of deciding which of the two tests should be used in the context of the ECMR. It is a matter for the Council of Ministers to determine whether it is appropriate to switch from the dominance standard to SLC; the fact that many Member States and potential acceding states have adopted the dominance test may mean that there is an inclination to retain the existing wording of Article 2 of the ECMR, but that is not an issue that I want to explore on this occasion.**
- **The important question for today is whether one test is 'better' than the other, and if so which? If one were to be designing a new system of merger control with a blank piece of paper in front of one, what test would one be likely to adopt?**
- **It is clear that many – probably most – mergers giving rise to competition concerns will be capable of substantive control whichever standard is applied: it is important not to exaggerate the differences between the dominance and the SLC tests. Many years of decision-making under the ECMR have shown that there is a high degree of agreement between the Commission and the competition authorities in other jurisdictions – in particular with the DoJ and the FTC in the US – in the overwhelming majority of cases. The different tests do not, themselves, give rise to serious friction. It is also clear that there will always be some cases where different authorities reach different conclusions – whether they are**

applying different tests or the same one – for the simple reason that a particular transaction may have a quite different impact from one state or region to another.

Specifically there seems to be no significant difference under the dominance standard in the EC and the SLC test in the US, in relation to:-

- Merger to monopoly/single firm dominance/unilateral effects
- Merger to oligopoly/collective dominance/coordinated effects

The analysis of these situations is, generally speaking, the same under each test. The *Airtours* judgment of the Court of First Instance of 6 June 2002 has provided clarity as to the current content of the collective dominance doctrine: it would appear to apply to the classic case of an oligopolistic market which is conducive to tacit coordination. The *indicia* of such a market are well known: homogeneous products, mature market, high barriers to entry, little buyer power, low technology products, high transparency, a credible prospect of retaliation which disciplines the oligopolists etc. Of course, *Airtours* will not necessarily be the final word on the collective dominance doctrine: no doubt there will be further cases in the future that test the doctrine further; however, for the time being it seems to be clear that collective dominance applies to the type of market just described: it does not appear to apply more broadly, and in particular it does not seem to capture cases in which one firm in an oligopoly is able to benefit from *unilateral* behaviour, as opposed to the mutually interdependent behaviour that occurs in the case of tacit coordination. In so far as the Commission's decision in *Airtours*, in particular at paragraph 54, was intended to 'stretch' collective dominance to cover such a situation, the CFI seems clearly to have rejected such an approach (it would have been helpful if the CFI could have dealt with this point specifically rather than be implication).

- The critical question therefore, given the version of collective dominance adumbrated by the CFI in *Airtours*, is whether there are some mergers that cannot be controlled under the dominance standard – even where dominance extends to '*Airtours* collective dominance' – and yet which are the subject of legitimate economic concern to competition authorities. Is there a third type of case which lies beyond single firm and/or collective dominance? Is there an 'empty box' which Article 2(3) of the ECMR does not address? If there is, does the SLC test cover it?
- Without going into the economics of this – and clearly this is a matter for economists rather than lawyers – it seems to me that it is plausible that there are some cases in the empty box, although it would be useful to conduct empirical research, across numerous jurisdictions, to find out quite how many.

- The important question would appear to be whether it is possible in some circumstances for a single firm, which is not dominant in the sense in which that term is used in EC law, to derive benefits from unilateral behaviour on the market, and where the market does not have those characteristics that render it conducive to tacit coordination.
 - For example there are many markets for branded goods and services which are concentrated – there may be as few as two or three players – and yet which are competitive: in other words, markets which do not lend themselves to tacit coordination. A three to two merger in such a market may not lead to single firm dominance, and does not seem to give rise to ‘*Airtours* collective dominance’, and yet there is a possibility that one of the remaining players may be able unilaterally to exercise market power. This case could be caught only by an extension of the collective dominance theory beyond the judgment of the CFI in *Airtours*. The SLC test would appear – at least linguistically – to capture this situation quite comfortably: post merger there may be substantially less competition.
 - In innovation markets in which technological rivalry is important, where the Schumpeterian gale of creative destruction blows strongly, a three to two merger might be viewed in just the same way: post merger there may be no single dominant firm, and the market hardly conforms to the *Airtours* model of collective dominance; however, there may be substantially less competition in such a market if one of the main potential entrants is eliminated.
 - There are various cases in a range of jurisdictions where mergers were investigated which were not struck down under a dominance test but which might have been or were under the SLC test. Possible examples are *Woolworths/Safeways* (Australia), *Qantas/Ansett* (Australia), *New Zealand Progressive Enterprises* (New Zealand), *Babyfoods* (US), *Airtours/First Choice* (EC), *Lloyds TSB/Abbey National* (UK). No doubt there are others. It is true that in the Australian and New Zealand cases the applicable laws did not apply to collective dominance but only to single-firm dominance: but would even a collective dominance doctrine have captured those cases?
- An important question is whether the concept of dominance, and more specifically the concept of collective dominance, can be ‘adapted’ to deal with ‘third box’ cases such as these, assuming that they really are beyond the scope of the existing case-law under the ECMR? In my view, unless and until the CFI and/or, in the final resort, the ECJ take a further look at collective dominance, some or all of these cases fall outside the test in the ECMR; but they could be caught under the SLC standard.

- A related question is whether, even if the dominance standard can be adapted to catch these cases, it is *appropriate* to ‘adapt’ the test in this way. Would it not better to adopt a formulation that is more appropriate to the policy objective in question? It seems to me that there is a danger that one introduces intellectual dishonesty into the equation if one distorts words to the point where they no longer carry their natural meaning. If the truth is that a competition authority wishes to apply the standard of SLC, albeit working with the wording of the ECMR, I think it better that the wording should be changed accordingly: the danger is that what will actually happen is that the word ‘dominance’ will be tortured until it confesses that it means something other than it says.