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Non-Horizontal Mergers: A European Perspective

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Abstract

In the last few years, the assessment of non-horizontal mergers in the European Union (“EU”) has evolved considerably. There is now a consistent body of jurisprudence and administrative decisions on the assessment of vertical and conglomerate concentrations. The goal pursued is consumer welfare; the potential benefits of non-horizontal mergers are recognized and sound economic thinking is relied upon in identifying those instances where such mergers could lead to anti-competitive effects. Several developments have significantly contributed to this evolution. Two judgments of the European Courts have necessarily to be mentioned first: in 2004 the European Court of Justice (“ECJ”) established general principles on the assessment of non-horizontal mergers in the *Commission v. Tetra Laval BV* (“Tetra/Sidel”) judgment, which were completed and made operational by the Court of First Instance (“CFI”) one year later in its judgment in *General Electric Co. v. Commission* (“GE/Honeywell”). Second, an amended Merger Regulation entered into force in May 2004. This introduction of a new test, which no longer requires proof that a merger will lead to dominance before allowing intervention to prevent consumer harm, is particularly relevant for non-horizontal mergers. Third, the European Commission (“the Commission”), in November 2007, adopted guidelines on the assessment on non-horizontal mergers which, within the legal framework set up by the Courts, attempt to develop an economically sound approach for the analysis of vertical and conglomerate concentrations. Finally, during this period, the Commission has dealt with several vertical and conglomerate mergers in its enforcement decisions, which have allowed it to already apply and refine its policy in a number of individual situations. This Article describes in detail and comments on all of these developments, both from a legal and from a policy perspective.

NON-HORIZONTAL MERGERS: A EUROPEAN PERSPECTIVE

*Carles Esteva Mosso**

INTRODUCTION

In the last few years, the assessment of non-horizontal mergers in the European Union (“EU”) has evolved considerably. There is now a consistent body of jurisprudence and administrative decisions on the assessment of vertical and conglomerate concentrations. The goal pursued is consumer welfare; the potential benefits of non-horizontal mergers are recognized and sound economic thinking is relied upon in identifying those instances where such mergers could lead to anti-competitive effects.

Several developments have significantly contributed to this evolution. Two judgments of the European Courts have necessarily to be mentioned first: in 2004 the European Court of Justice (“ECJ”) established general principles on the assessment of non-horizontal mergers in the *Commission v. Tetra Laval BV* (“*Tetra/Sidel*”) judgment,¹ which were completed and made operational by the Court of First Instance (“CFI”) one year later in its judgment in *General Electric Co. v. Commission* (“*GE/Honeywell*”).² Second, an amended Merger Regulation³ entered into force in May 2004. This introduction of a new test, which no longer requires proof that a merger will lead to dominance before allowing intervention to prevent consumer harm, is particularly relevant for non-horizontal mergers. Third, the European Commission (“the Commission”), in November 2007, adopted guidelines on the assessment on non-horizontal mergers which, within the legal framework set up by the Courts, attempt to develop an economically sound approach for the analysis of vertical and con-

* Head of Unit for Merger Policy and Scrutiny. Directorate General for Competition. European Commission. The views expressed are personal and cannot be attributed to the European Commission. I would like to thank Guillaume Loriot, Stephen Ryan and Kay Parplies, from DG Competition, as well as Giuseppe Conte, from the Legal Service of the Commission, for their comments and contributions to this Article.

1. *Commission v. Tetra Laval BV*, Case C-12/03 P, [2005] E.C.R. I-987.

2. *Gen. Elec. Co. v. Commission*, Case T-210/01, [2005] E.C.R. II-5575.

3. Council Regulation No. 139/04, O.J. L 24/1 (2004) (on the control of concentrations between undertakings).

glomerate concentrations.⁴ Finally, during this period, the Commission has dealt with several vertical and conglomerate mergers in its enforcement decisions, which have allowed it to already apply and refine its policy in a number of individual situations.

This Article describes in detail and comments on all of these developments, both from a legal and from a policy perspective.

I. *THE TETRA/SIDEL AND GE/HONEYWELL JURISPRUDENCE ON NON-HORIZONTAL MERGERS*

In the seventeen years of application of the Merger Regulation, the ECJ and the CFI have ruled on the interpretation of many of its provisions. However, while they had dealt already with a number of Commission decisions, including an analysis of non-horizontal effects,⁵ the European Courts did not need to develop jurisprudence on the substantive assessment of such cases until quite recently. The appeals against the Commission's prohibition decisions of the *Tetra/Sidel* and *GE/Honeywell* transactions provided the first opportunity to develop a consistent body of principles in this area of merger law. The main elements of this jurisprudence are presented below.

A. *The Interpretation of the Merger Test and the Standard of Proof for Non-Horizontal Mergers*

At the time of the adoption of the *Tetra/Sidel* and *GE/Honeywell* decisions, Article 2 of the Merger Regulation provided that the European Commission had to appraise mergers with a view to establishing whether or not they would "create or strengthen a dominant position as a result of which competition would be significantly impeded in the EU market or a substantial part of it."⁶ One of the key issues dealt with by the *Tetra/Sidel* appeal was the definition of the standard of proof that this test imposed

4. See Commission Notice, Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings (Nov. 28, 2007), available at <http://ec.europa.eu/comm/competition/mergers/legislation/nonhorizontalguidelines.pdf> [hereinafter Guidelines].

5. See, e.g., *MCI, Inc. v. Commission*, Case T-310/00, [2004] E.C.R. II-3253; *BaByliss SA v. Commission*, Case T-114/02, [2003] E.C.R. II-1279; *Royal Philips Elec. NV v. Commission*, Case T-119/02, [2003] E.C.R. II-1433; *Endemol Entm't Holding BV v. Commission*, Case T-221/95, [1999] E.C.R. II-1299.

6. Council Regulation No. 4064/89, art. 2, O.J. L 257/90, at 13 (1990) (originally published in O.J. L 395 (1989)) (on the control of concentrations between undertakings).

on the Commission, in particular in the context of the assessment of a conglomerate merger.⁷

The Commission argued that Article 2 of the Merger Regulation requires a “balance of probabilities” assessment of all proposed mergers, irrespective of the type of merger being assessed.⁸ The Commission, indeed, considered that Article 2 of the Merger Regulation created a symmetrical obligation on the Commission to authorize a concentration if it is not likely to create or strengthen a dominant position and to prohibit it if it is likely to create or strengthen it.⁹ This reflected, in the Commission’s view, an underlying choice by the Community legislator, clearly apparent in the terms and structure of the Regulation, equally to protect, on the one hand, the private interests of the merging parties and, on the other hand, the public interest in maintaining effective competition and the interests of consumers.

The CFI, in its judgment¹⁰ annulling the Commission’s decision,¹¹ made it clear that the Merger Regulation applies equally to all types of mergers:

The Regulation, particularly in Article 2(2) and (3), does not draw any distinction between, on the one hand, merger transactions having horizontal and vertical effects and, on the other hand, those having a conglomerate effect. It follows that, without distinction between those types of transactions, a merger can be prohibited only if the two conditions laid down in Article 2(3) are met.¹²

However, the CFI also stated that “[s]ince the effects of a conglomerate-type merger are generally considered to be neutral, or even beneficial, for competition on the markets concerned . . . the proof of anti-competitive conglomerate effects of such a merger calls for a precise examination, supported by convincing evidence, of the circumstances which allegedly produce those effects.”¹³ This sentence, while not explicitly imposing a different

7. *Tetra Laval*, [2005] E.C.R. I-987.

8. *Id.* ¶ 3.

9. *Id.* ¶ 29.

10. *Tetra Laval BV v. Commission*, Case T-5/02, [2002] E.C.R. II-4381.

11. *See* Commission Decision No. COMP/M.2416, O.J. L 43/13 (2004) (*Tetra Laval/Sidel*).

12. *Tetra Laval*, [2002] E.C.R. II-4381, ¶ 146.

13. *Id.* ¶ 55.

assessment standard for conglomerate mergers, opened a discussion as to whether the CFI was actually establishing a distinction as to the burden of proof applying to them.

The ECJ, in ruling on the assessment standard, does not make any distinction on the applicability of the Regulation to different types of mergers. It also seems to confirm the symmetrical character of the test by indicating that, in conducting a prospective merger analysis, the Regulation requires an examination of “various chains of cause and effect with a view to ascertaining which of them are the most likely.”¹⁴ This symmetrical character of the merger test appears to have been later confirmed by the CFI in the *GE/Honeywell* judgment, which indicated that the Merger Regulation does not establish any presumption as to the compatibility or incompatibility of mergers and that: “[i]t is not the case that the Commission must find in favour of a concentration falling within its jurisdiction in a case in which it might entertain doubts but rather that it must always make an actual decision one way or another.”¹⁵

As to the burden of proof applying to conglomerate mergers, the ECJ notes that the CFI’s reference to convincing evidence “by no means added a condition relating to the . . . standard of proof but merely drew attention to the essential function of evidence, which is to establish convincingly the merits of an argument or . . . of a decision.”¹⁶ However, the ECJ added that:

The analysis of a “conglomerate-type” concentration is a prospective analysis in which, first, the consideration of a lengthy period of time in the future and, secondly, the leveraging

14. *Tetra Laval*, [2005] E.C.R. I-987, ¶ 43. The European Court of Justice (“ECJ”) appears not to have followed the Opinion of Advocate General Tizzano that had suggested an asymmetric test, requiring the Commission to be persuaded that the operation would “very probably” create or strengthen a dominant position. In particular, according to Advocate General Tizzano, a concentration should be authorized in cases “where it is especially difficult to foresee the effects of the notified transaction and where it is therefore impossible to arrive at a clear distinct conviction that the likelihood that a dominant position will be created or strengthened is *significantly* greater or less than the likelihood that such a position will not be created or strengthened.” Opinion of Advocate General Tizzano, *Commission v. Tetra Laval BV*, Case 12/03 P, [2004] E.C.R. I-987, ¶¶ 74, 76.

15. *Gen. Elec. Co. v. Commission*, Case T-210/01, [2005] E.C.R. II-5575, ¶ 61. The same symmetric interpretation of a substantive appraisal standard was applied afterwards by the CFI to Article 81. See *GlaxoSmithKline Servs. Unlimited v. Commission*, Case T-168/01, [2006] E.C.R. II-2969, ¶ 249.

16. *Tetra Laval*, [2005] E.C.R. I-987, ¶ 41.

necessary to give rise to a significant impediment to effective competition mean that the chains of cause and effect are dimly discernible, uncertain and difficult to establish.¹⁷

That being so, the quality of the evidence produced by the Commission in order to establish that it is necessary to adopt a decision declaring the concentration incompatible with the common market is particularly important, since that evidence must support the Commission's conclusion that, "if such a decision were not adopted, the economic development envisaged by it would be plausible."¹⁸ The ECJ, therefore, seems to draw a distinction between different types of mergers in terms of the level of evidence necessary to prove their anticompetitive effects. In those cases where the anticompetitive effects of the merger are not immediate, but rather depend on the effects that the conduct of the merged entity will have in the market in the future, for instance through the foreclosure of competitors (or "leveraging" as the ECJ says), such evidence should be "particularly important."

While maintaining the same assessment standard for all types of mergers, it seems reasonable to distinguish the level and quality of evidence necessary to prove different theories of harm, as the ECJ does. It would generally be easier to demonstrate the likely anticompetitive effects linked to a horizontal merger removing a direct competitive constraint, for instance, than those linked to theories that require several more steps of reasoning and that would lead to anticompetitive effects—not immediately—but at a certain point in the future. This raises the question, however, of whether all non-horizontal mergers would only impede effective competition in an indirect way, therefore requiring such "particularly important" evidence to be put forward. Indeed, competition concerns raised in non-horizontal mergers often result from the risk of foreclosure of actual competition. In such cases the theory of harm relies on the fact that the merged entity is likely to have the ability and incentives to engage in certain conduct in the future (e.g. refusal to deal, tying) that would raise the cost of rivals, ultimately leading to anticompetitive effects. However, there are also non-horizontal cases in which there is a much more direct link between the

17. *Id.* ¶ 44.

18. *Id.*

merger and the detrimental effect on competition. For instance, a vertical merger may have direct anti-competitive effects by allowing a firm to gain access to commercially sensitive information concerning its rivals. Or the merger itself, with no specific action of the merged entity required, may already change the incentives of potential entrants into a certain market (for instance requiring a two-level entry post-merger) and lead to immediate anti-competitive effects.¹⁹ In view of this, it seems difficult to conclude that the *Tetra/Sidel* judgment has established a higher burden of proof for all non-horizontal mergers per se. It is rather more plausible to conclude that the level and quality of evidence will depend very much on the nature of the theory of harm advanced by the Commission, and in particular the period of time which the theory anticipates will elapse before the anti-competitive effects are likely to materialize.

Looking ahead, the operational conclusion from the above would seem to be that, in order to apply the test in Article 2 of the Merger Regulation, the Commission must apply a “balance of probabilities” standard and, therefore, in order to prohibit a merger or request remedial action, it should demonstrate that a significant impediment of effective competition is more likely than not.²⁰ This assessment standard applies equally to both horizontal and non-horizontal mergers.

With regard to the burden of proof, the Commission must in all cases provide convincing evidence to sustain the conclusion that the test is, or is not, met. The level and quality of the evidence necessary to meet such a burden will largely depend on the theory of harm that the Commission is advancing. A distinction can, in that regard, be made between those concentrations that would immediately have an anticompetitive effect, such as a horizontal merger, or a non-horizontal merger with an immediate effect, and those operations having a less immediate impact on competition, such as vertical or conglomerate mergers that would lead to foreclosure of actual rivals. Such a distinction, however, is more a distinction of degree than an absolute one. The more speculative the theory of harm advanced, or the

19. See Claes Bengtsson et al., *The Substantive Assessment of Mergers*, in EU COMPETITION LAW: VOL. II: MERGERS & ACQUISITIONS 312-13 (Gotz Drauz & Christopher Jones eds., 2006).

20. See Opinion of Advocate General Kokott, Bertelsmann AG, Sony Corporation of America v. Commission, Case C-413/06 (ECJ Dec. 13, 2007) (not yet reported).

longer the time-frame for competitive effects which the theory forecasts, the more difficult it will be for the Commission to meet the test of Article 2.

B. *The Assessment of Foreclosure Theories*

In the *GE/Honeywell* judgement, the Court of First Instance develops the general principles established by the European Court of Justice and sets out, in a more detailed manner, the different steps in the assessment that the Commission should carry out, and examines how the Commission went about this assessment in the particular case. The CFI's focus is on the foreclosure theories which, in the form of alleged likelihood of future refusal to deal or bundling by the merged entity, were at the core of the Commission's case.²¹

The CFI starts by acknowledging that the anti-competitive effects alleged by the Commission "would have only followed from the merger in so far as the merged entity had adopted certain behaviour after the merger In those circumstances, the Commission had the onus to provide convincing evidence to support its conclusion that the merged entity would probably behave in the way foreseen."²² This would require, first, that the Commission prove the capacity or ability to engage in such practices and second, that it would prove that it was likely that the merged entity would engage in such conduct. Once ability and likelihood have been established, the Commission is required to establish that those practices would have created or strengthened, in the relatively near future, a dominant position on some of the markets concerned.²³ As we will see, this three-step analysis (ability, likelihood/incentives, effects) will become the organizing principle for the Commission assessment of non-horizontal mergers and hence forms the basis for the analytical framework set out in its non-horizontal guidelines.

21. The Commission decision, however, was upheld by the Court of First Instance ("CFI") relying on purely horizontal theories of harm. Indeed, the CFI concluded that the conclusion that the operation would have strengthened GE's dominant position in the market for jet engines for large regional aircraft and would have created a dominant position in the markets for engines for corporate jet aircraft and small marine gas turbines were sufficient, in the absence of adequate remedies, to justify a finding of incompatibility. See *Gen. Elec.*, [2005] E.C.R. II-5575, ¶¶ 732-34.

22. *Id.* ¶¶ 68-69 (referring to conglomerate effects); see *id.* ¶ 295 (referring to vertical effects).

23. See *id.* ¶¶ 327, 405 (referring specifically to conglomerate practices).

1. Ability

Certain conditions have to be satisfied for a merged entity to be able to engage successfully in foreclosure practices. In the *GE/Honeywell* judgment, the CFI particularly examines some of these conditions in the section dealing with the ability of the merged entity to engage in so-called “pure” and “technical” bundling practices, with regard to the sale of aircraft engines, avionics and non-avionics products.

First of all, the CFI analyzes whether the market characteristics and the behavior of customers would allow the merged entity to engage in those practices. In the examination of pure bundling, for instance, the CFI notes that only in some situations is the customer for engines, avionics and non-avionics products the same. Indeed, there are situations where the engine and/or some avionics are already chosen by the air-framer and the airline buying the aircraft has only a limited choice between additional avionics products. In these situations, the ability to engage in bundling practices is limited or even non-existent. The CFI also notes that, in many instances, the selection of engines and avionics takes place at different points in time. While this circumstance may not prevent bundling, it would certainly make it much more difficult for it to succeed.²⁴

Second, the CFI examines whether the Commission had established that the merged entity would have sufficient market power in one of the bundled product markets in order to be able to impose the bundle successfully on its customers. This analysis would require an examination of whether the customers of the bundling product would have alternatives, and in particular whether substitute products would be available in the market. Even in situations where the bundle would include GE engines, and despite the fact that the CFI was satisfied that GE held a dominant position in this market, the CFI requires the Commission to establish that customers would have lost all residual power to refuse the imposition of the bundling practices.²⁵

2. The Likelihood of Foreclosure Practices

Once the ability of the merged entity to engage in certain

24. *Id.* ¶¶ 407-16.

25. *Id.* ¶¶ 422-23.

practices is established, there are several means, according to the CFI, to prove the likelihood of such practices actually taking place. First of all, documents attesting to the settled intention of the board of directors of one of the merging parties to engage in certain practices post-merger could be considered convincing evidence.²⁶

But most often, the likelihood of certain anti-competitive practices occurring will depend on the economic incentives that the merged entity will have to engage in them. Such incentives can be gauged by comparing the likely costs to the merged entity of such practices with the benefits that they would be likely to produce. In view of this, economic studies assessing such trade-offs are often considered by the CFI as a necessary means to convincingly demonstrate likelihood. The CFI, for instance, states: “[i]n some cases, such evidence may consist of economic studies establishing the likely development of the market situation and demonstrating that there is an incentive for the merged entity to behave in a particular way.”²⁷

It adds, however, that:

[T]he absence of evidence of that type is not in itself decisive. In particular, in a situation in which it is obvious that the commercial interests of an undertaking militate predominantly in favour of a given course of conduct, such as making use of an opportunity to disrupt a competitor’s business, the Commission does not commit a manifest error of assessment in holding that it is likely that the merged entity will actually engage in the conduct foreseen. In such a case, the simple economic and commercial realities of the particular case may constitute the convincing evidence required by the case-law.²⁸

On the basis of these considerations, the CFI considered that the Commission’s analysis of the incentives of the merged entity to engage in input foreclosure in the engines starter market was “persuasive.” Indeed, the fact that the merger would lead to the vertical integration of Honeywell—which was de facto the only supplier of engine starters, a relative low-cost but crucial component of aircraft engines—and GE—which already held a dominant position in the market for the manufacture of

26. *Id.* ¶¶ 332-33; *see also id.* ¶¶ 439-43.

27. *Id.* ¶ 296.

28. *Id.* ¶ 297.

such engines for large commercial aircraft—was sufficient to conclude that it would be in the commercial interests of the merged entity to use its power as the unavoidable supplier of these products as a means of disrupting its competitors' engine production. In particular, the CFI noted that the profits that the merged entity could make by selling engine starters to GE's competitors would be minimal compared to the profits it could obtain by increasing its share of the market of engines for large commercial aircraft at the expense of these competitors.²⁹

In the absence of any of the types of evidence mentioned in the previous paragraphs, the CFI is unlikely to find that the Commission has proved to a sufficient degree the likelihood of particular conduct taking place in the market post-merger. In fact, the CFI considered that the Commission had not provided such evidence in this particular case and had not, therefore, sufficiently established the likelihood that the merged entity would engage in the bundling of jet engines with avionics and non-avionics products, or in other practices aimed at exploiting the commercial interests of the GE group in order to promote sales of Honeywell's products.³⁰ In particular, the CFI noted in several paragraphs of the judgment that such practices would have probably involved certain costs for the merged entity and "would have been rational commercial behaviour following the merger only in so far as the revenues which the merged entity was likely to derive from those practices would have offset that potential cost."³¹ As the Commission had not provided economic studies comparing, at least on the basis of reasonable estimates, any such costs with any such revenues, it could not infer that the practices in question were likely.

3. The Specific Issue of Legal Disincentives

In assessing the likelihood that the merged entity would engage in certain practices, a particularly controversial question is how the Commission should take into account the possible illegality of such practices. Foreclosure practices could, indeed, in some instances be contrary to national and/or EU law and, in particular if the merged entity holds a dominant position, they

29. *See id.* ¶ 299.

30. *Id.* ¶¶ 470-73.

31. *Id.* ¶¶ 338-39; *see also id.* ¶¶ 444-62.

could constitute an abuse under Article 82 of the EU Treaty.³² Does this mean that the Commission should exclude the possibility that the merged entity might engage in such behavior or, taking the contrary view, should such considerations play any role in an assessment under the Merger Regulation? The ECJ and the CFI, in *Tetra/Sidell* and *GE/Honeywell*, have provided slightly different replies to this question.

In the *Tetra/Sidel* judgment, the CFI, when assessing the likelihood that Tetra would engage in leveraging, stated the following:

When the Commission, in assessing the effects of such a merger, relies on foreseeable conduct which in itself is likely to constitute abuse of an existing dominant position, it is required to assess whether, despite the prohibition of such conduct, it is none the less likely that the entity resulting from the merger will act in such a manner or whether, on the contrary, the illegal nature of the conduct and/or the risk of detection will make such strategy unlikely. While it is appropriate to take account . . . of incentives to engage in anti-competitive practices . . . the Commission must also consider the extent to which those incentives would be reduced, or even eliminated, owing to the illegality of the conduct in question, the likelihood of its detection, action taken by the competent authorities, both at Community and national level, and the financial penalties which could ensue.³³

As the Commission had not carried out such an assessment in the contested decision, the CFI considered that its findings based on anti-competitive leveraging practices could not be upheld.

In its appeal of the CFI judgment, the Commission argued that the requirement to conduct such an assessment was contrary to the purpose of the Merger Regulation. Indeed, if Article 82 were sufficient to prevent abuses, it would not have been necessary to make provision for ex ante control of concentrations. It also argued that a requirement to carry out such an assessment presented the Commission with virtually insuperable legal and practical obstacles. It required the Commission to examine the propensity of firms to comply with the law, thereby inevitably depriving such firms of the benefit of the presumption of inno-

32. *Id.* ¶ 86.

33. *Tetra Laval BV v. Commission*, Case T-5/02, [2002] E.C.R. II-4381, ¶ 159.

cence. Moreover, the risk of detection would depend on the strictness of competition policy and enforcement in each Member State and would, therefore, be very difficult to assess in accordance with the standard of proof required by the CFI.

The ECJ ruled in favor of the Commission on this issue. It clearly stated that:

The Court of First Instance erred in law in rejecting the Commission's conclusions . . . on the sole ground that the Commission had, when assessing the likelihood that such conduct might be adopted, failed to take account of the unlawfulness of that conduct and, consequently, of the likelihood of its detection, of action by the competent authorities, both at Community and national level, and of the financial penalties which might ensue.³⁴

The ECJ accepted that the Commission should assess both the incentives of the merged entity to adopt certain conduct and the factors liable to reduce, or even eliminate those incentives, including the possibility that the conduct would be unlawful. However, to perform such an analysis in the manner prescribed by the CFI "would run counter to the Regulation's purpose of prevention."³⁵ Moreover, such an analysis, by being too speculative, would prevent the Commission from basing its assessment on a purely factual and economic basis.³⁶

Surprisingly, and despite this conclusion, the CFI again required the Commission in the *GE/Honeywell* judgment to conduct an analysis of the possible illegality of the conduct in which the merged entity could engage. In so doing, the CFI interpreted that the ECJ's judgment in *Tetra/Sidel* had not excluded the need to perform such an analysis. In the CFI's view, the ECJ's judgment did not "require to establish that the conduct foreseen in the future will actually constitute an infringement of Article 82 or that, if that were to be the case, that infringement would be detected and punished." It simply required the Commission to conduct a "summary analysis based on the evidence available to it."³⁷ As such an analysis had not been performed in the case at hand, the CFI considered that the Commission had not estab-

34. *Commission v. Tetra Laval BV*, Case C-12/03 P, [2005] E.C.R. I-987, ¶ 78.

35. *Id.* ¶ 75.

36. *See id.* ¶ 77.

37. *Gen. Elec. Co. v. Commission*, Case T-210/01, [2005] E.C.R. II-5575, ¶ 304.

lished the likelihood that the merged entity would engage in certain practices, such as vertical foreclosure in the engine starters market or some types of bundling. As we have seen, in the absence of the legal disincentive, the CFI had considered the analysis of the Commission on the likelihood of such practices to be “persuasive.”

To conclude on this point, in *GE/Honeywell* the CFI seems to have followed a middle road between the two possible extreme solutions to this difficult issue: either requiring the Commission to conduct a full analysis into the possible disincentive that the illegality could represent, as the CFI had previously ruled in *Tetra/Sidel*, with all the difficulties that such analysis might entail; or excluding completely this type of analysis on the basis that the Merger Regulation is a preventive instrument, adopted precisely to avoid illegal conduct. There is at least clarity—and some merits—in both these solutions. It is, however, less easy to say with certainty what are the obligations that the CFI’s intermediate line now imposes on the Commission. And it is certainly not easy to reconcile the line most recently adopted by the CFI with the ECJ’s reasoning in *Tetra/Sidell* and, in particular, to understand how a summary analysis would not run counter to the Regulation’s underlying purpose of prevention, or indeed why it would be less speculative than an analysis based on full evidence. For the time being, however, this is the most recent jurisprudence on this issue and, as such, it will have to be taken into account by the Commission in the assessment of most non-horizontal mergers (see below, in the description of the guidelines, how the Commission plans to apply this jurisprudence in practice).

4. Effects

The Commission should not confine itself to establishing the ability and likelihood of foreclosure theories, but should also demonstrate that such foreclosure would produce anticompetitive effects. Indeed, the Merger Regulation is based on a consumer welfare standard and, therefore, the exclusion or marginalization of competitors in a certain market is not of itself sufficient to establish a finding of incompatibility. Rather, it should be proved that, by raising the costs of one or more competitors, or excluding them from the market, the merger would

ultimately have an anticompetitive effect and harm consumer welfare.

The *GE/Honeywell* judgment restates the need to prove anti-competitive effects but, as it had already rejected the Commission's findings due to the lack of evidence on the ability or likelihood of the merged entity to engage in foreclosing conduct, it did not need to examine the Commission's assessment of the effects. The judgment contains only one relevant consideration to this regard, which requires the Commission to assess the effects on each relevant market separately.³⁸

II. THE ASSESSMENT OF EFFECTS UNDER THE NEW MERGER REGULATION

It should be examined whether the new test of the Merger Regulation, which establishes in Article 2 that the Commission has to assess whether a concentration "would significantly impede effective competition, in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position,"³⁹ could have any impact on the jurisprudence; both cases presented above were based on the previous wording of that article.

The change in the test was generally explained as an attempt, first, to shift from a more structural paradigm, where the notion of dominance was central to the analysis, to a more effects-based approach, where the impact of the concentration in market outcomes (price, output, innovation, etc.) would be at the center of the Commission's analysis. Second, the new test was also intended to eliminate any possible enforcement "gap" by covering those mergers that, while not creating or strengthening a dominant position, would nevertheless cause consumer harm.

This change is particularly relevant to the assessment of non-horizontal mergers. In effect, the new test no longer requires demonstrating that the effects of the concentration would be the creation or strengthening of a dominant position but rather that it would significantly impede effective competition. And indeed, in a number of instances, the integration between a company with market power in one market with another com-

38. *See id.* ¶ 362.

39. Council Regulation No. 139/2004, art. 2, O.J. L 24/1, at 7 (2004).

pany operating in a vertically related or neighboring market could lead to consumer harm in the latter one, without the merged entity acquiring a dominant position in this latter market.

This is particularly the case for “raising rivals’ costs” theories of harm.⁴⁰ Indeed, the concern with regards to raising rivals’ costs, be it in the more direct form of input foreclosure or in the more indirect one of customer foreclosure, is not that a dominant position will be created as a result of vertical integration, but rather that such structural change will negatively affect market outcomes, for instance leading to higher prices. These theories of harm, as will be explained below, are central to the Commission’s guidelines on the assessment of non-horizontal mergers.

It is curious to see, in retrospect, that the debate about whether to modify the test of the Merger Regulation did not focus more on these possible “gaps” in the previous test. Rather, that debate was centered on the perceived gap with regard to non-coordinated effects arising from horizontal mergers in oligopolistic markets.⁴¹ Recital 25 of the Merger Regulation, which refers to the amendment of the test, does not exclude that the new test would also be applicable to non-horizontal settings.⁴² Indeed, by indicating that the new test would cover “the anti-competitive effects of a concentration resulting from the non-coordinated behaviour of undertakings which would not have a dominant position on the market concerned,” it seems clearly to include non-coordinated foreclosure practices resulting from a non-horizontal merger, even when the entity would not have a dominant position on the market concerned.⁴³

III. *THE NON-HORIZONTAL MERGER GUIDELINES*

In November 2007 the Commission adopted guidelines on the assessment of non-horizontal mergers,⁴⁴ setting out the analytical approach it takes in assessing the likely competitive impact

40. See DAMIEN NEVEN, *CURRENT COMPETITION LAW*, VOL. V, at 394-98 (Philip Marsden et al. eds., 2007).

41. See, e.g., Claus-Dieter Ehlermann et al., *Unilateral Effects: The Enforcement Gap Under the Old EC Merger Regulation*, 28 *WORLD COMPETITION L. & ECON. REV.* 193 (2005).

42. See Commission Regulation No. 139/2004, pmbl. 25, O.J. L 24/1, at 4 (2004).

43. See *id.*

44. See generally Guidelines, *supra* note 4.

of vertical and conglomerate mergers within the legal framework established by the Courts. The main goal of these guidelines is to provide guidance to companies contemplating this type of merger, but at the same time, as with any other interpretative Notice, they also contribute to increasing the coherence of the Commission's enforcement practice and to providing enhanced legal predictability. They complement the existing guidelines on the assessment of horizontal mergers, which deal with mergers between companies who are actual or potential competitors in the same relevant market(s).⁴⁵

A. *The Adoption Process of the Non-Horizontal Guidelines*

The Commission, as it did before adopting the horizontal guidelines, prepared the adoption of the non-horizontal ones by extensively reviewing the relevant economic theory and literature.⁴⁶ It also sought advice from its own Economic Advisors Group on Competition Policy ("EAGCP"), which proposed 10 principles on which the non-horizontal guidelines should be based.⁴⁷ The drafting of the guidelines resulted from a joint effort within the Directorate General for Competition ("DG Competition") involving the Merger Network, the Chief Economist Team and the Competition Policy Directorate, and benefited from comments of other services in the Commission as well as from national competition authorities.

As it usually does before adopting any major interpretative Notice, the Commission published draft guidelines in February 2007.⁴⁸ The publication by the Commission of guidelines in a draft form is intended to give to interested parties the opportunity to express their views and make comments. In view of the

45. Commission Communication, O.J. C 31/03 (2004) (on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings).

46. See generally JEFFREY CHURCH & UNIV. OF CALGARY DEP'T OF ECON., *THE IMPACT OF VERTICAL AND CONGLOMERATE MERGERS ON COMPETITION* (2004); RBB ECONOMICS, *THE EFFICIENCY-ENHANCING EFFECTS OF NON-HORIZONTAL MERGERS* (2005).

47. ECON. ADV. GROUP FOR COMPETITION POL'Y ("EAGCP"), *NON-HORIZONTAL MERGER GUIDELINES: TEN PRINCIPLES* (2006), available at http://ec.europa.eu/comm/competition/mergers/legislation/non_horizontal_guidelines.pdf.

48. See Draft Commission Notice, Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings, (Feb. 13, 2007) [hereinafter Draft Guidelines], available at http://ec.europa.eu/comm/competition/mergers/legislation/non_horizontal_consultation.html.

relevance of this document for merger control policy, a three-month long consultation period was opened after publication, lasting until May 12, 2007.⁴⁹ Thirty-two comments were received in response to the public consultation,⁵⁰ mostly from the business and legal community. Many of these comments broadly praised the Commission's draft, but also raised concerns with regard to several areas or messages in the guidelines. Many also provided useful drafting suggestions. The general concerns raised by the draft guidelines are briefly summarized below.

As to the need for guidance, most respondents broadly welcomed the publication of guidelines. Only one respondent proposed not to issue guidelines because it considered that the existing case law under the revised Merger Regulation was too limited. Some other comments suggested that guidance be limited to vertical issues, and should not deal with possible conglomerate concerns.

As to the general principles, the suggestion of many comments was to emphasize further the potential efficiencies generated by non-horizontal mergers. In this regard, several respondents objected to the fact that the sections outlining potential scenarios of harm occupy substantially more space than the enumeration of potential pro-competitive effects of non-horizontal mergers. Others, while accepting that the focus of the guidelines should be on those cases that warrant an investigation rather than on those that do not raise problems, would nevertheless welcome that the efficiency enhancing aspects of non-horizontal mergers are emphasized further.

Some commentators also pointed out that economic theories that identify harm from non-horizontal mergers are less robust than equivalent theories for horizontal operations and, therefore, can be less reliable in defining policy. The fact that consumer harm does not result directly from the concentration but only from certain behavior from the merging firm, and therefore, the possibility to tackle such behavior through ex-post analysis, and in particular, by Article 82 TEU, is also, according

49. See *Commission Launches Public Consultation on Draft Non-Horizontal Merger Guidelines*, COMPETITION POL'Y NEWSLETTER, Spring 2007, at 16, available at http://ec.europa.eu/comm/competition/publications/cpn/cpn2007_1.pdf.

50. Comments received in response to a public consultation are available on the European Commission's Competition website, http://ec.europa.eu/comm/competition/mergers/legislation/non_horizontal_consultation.html.

to some commentators, a distinct feature of non-horizontal mergers.

In view of all the above, several papers advocated a degree of regulatory restraint in examining non-horizontal mergers (a “light-touch regulatory approach” as one contribution refers to it).⁵¹ Others conclude that a stricter standard of proof, or even a presumption of legality, should apply.⁵²

More specific comments and the reaction of the Commission to them will be presented in the sections of this Article describing the different parts of the guidelines.

B. *General Overview of the Commission’s Analysis of Non-Horizontal Mergers*

The guidelines are structured in four main parts: (i) a general overview, (ii) the definition of “safe harbours” in terms of market shares and concentration levels, (iii) the assessment of vertical mergers, and (iv) the assessment of conglomerate mergers.⁵³

The guidelines start by acknowledging, as one of the main messages in the introductory section, that there are differences between non-horizontal and horizontal mergers with regards to their impact on competition and that the former are generally less likely to give rise to competition concerns than the latter.⁵⁴ They also explain at length the reasons behind this difference.

First, unlike horizontal mergers, vertical or conglomerate mergers do not entail the loss of direct competition between the merging firms in the same relevant market. As a result, the main source of anti-competitive effects in horizontal mergers is absent from vertical and conglomerate mergers.⁵⁵

Second, vertical and conglomerate mergers typically pro-

51. See INT’L BAR ASS’N ANTITRUST COMM., IBA WORKING GROUP ON THE EUROPEAN COMMISSION’S DRAFT GUIDELINES ON THE ASSESSMENT OF NON-HORIZONTAL MERGERS 9-12, available at http://ec.europa.eu/comm/competition/mergers/legislation/files_non_horizontal_consultation/iba.pdf.

52. See LINKLATERS/CRA INT’L, THE EUROPEAN COMMISSION’S DRAFT GUIDELINES ON THE ASSESSMENT OF NON-HORIZONTAL MERGERS 4 (2007), available at http://ec.europa.eu/comm/competition/mergers/legislation/files_non_horizontal_consultation/linklaters.pdf.

53. See generally Guidelines, *supra* note 4.

54. *Id.* ¶ 11.

55. See *id.*

vide substantial scope for efficiencies.⁵⁶ A characteristic of vertical mergers and certain conglomerate mergers is that the activities and/or the products of the companies involved are complementary to each other.⁵⁷ The integration of complementary activities or products within a single firm may produce significant efficiencies and be pro-competitive.⁵⁸ For instance, in vertical mergers, efforts to increase sales at one level (e.g. by lowering price, or by stepping up innovation) will benefit sales at the other level.⁵⁹ Depending on the market conditions, integration may increase the incentive to carry out such efforts.⁶⁰ The internalization of double mark-ups after the vertical integration, (i.e. lowering the mark-up upstream may lead to increased sales not only upstream but also downstream and vice versa) is particularly taken into account in this context.⁶¹

The guidelines also acknowledge that vertical and conglomerate mergers may reduce transaction costs and allow for better coordination in terms of product design, the organization of the production process, investments in production factors along the value chain and the way in which the products are sold.⁶² Similarly, mergers which involve products belonging to a range of products that are generally sold to the same set of customers (be they complementary products or not) may give rise to customer benefits such as facilitating one-stop-shopping.⁶³

The main task of the guidelines, however, is to provide guidance in identifying those circumstances in which non-horizontal mergers may significantly impede effective competition or, in other words, change the ability and incentive to compete on the part of the merging companies and their competitors in ways that are likely to cause harm to consumers. The guidelines distinguish between two main ways in which non-horizontal merg-

56. *See id.* ¶ 13.

57. *See id.* Products or services are called "complementary" (or "economic complements") when they are worth more to a customer when used or consumed together than when used or consumed separately. A merger between upstream and downstream activities can be seen as a combination of complements which go into the final product; for instance, both production and distribution fulfill an indispensable role in getting a product to the market.

58. *See id.*

59. *See id.*

60. *See id.*

61. *See id.*

62. *See id.* ¶ 14.

63. *See id.*

ers may significantly impede effective competition: non-coordinated effects and coordinated effects.⁶⁴

Non-coordinated effects will principally arise when non-horizontal mergers give rise to foreclosure.⁶⁵ In the guidelines, the term “foreclosure” is used to describe any instance where actual or potential rivals’ access to supplies or markets is hampered or eliminated as a result of the merger, thereby reducing these companies’ ability and/or incentive to compete.⁶⁶ As a result of such foreclosure, the merging companies—and, possibly, some of its competitors as well—may be able to profitably increase the price charged to consumers or cause harm to consumers in other ways. These instances are referred to as “anticompetitive foreclosure.”

In assessing the likelihood of an anticompetitive foreclosure scenario, in line with what the jurisprudence has required (see above), the Commission will examine: first, whether the merged entity would have, post-merger, the ability to substantially foreclose a market; second, whether it would have the incentive to do so, and; third, whether a foreclosure strategy would have a significant detrimental effect on competition, thus causing harm to consumers.

In practice, these three factors are often examined together since they are closely intertwined. Nonetheless, the Commission finds it useful to make clear that, even though the merged entity may have the ability to foreclose, it may not have the incentive to do so. Moreover, even where the merged entity may have the ability and incentive to foreclose, this may not have a significant detrimental effect on consumers.

Coordinated effects arise where the merger changes the nature of competition in such a way that firms that previously were not coordinating their behavior, are now significantly more likely to coordinate and raise prices or otherwise harm effective competition.⁶⁷ A merger may also make coordination easier, more stable or more effective for firms, which were coordinating prior to the merger.⁶⁸

64. *See generally id.*

65. *See id.* ¶ 18.

66. *See id.*

67. *See id.* ¶ 19.

68. *See id.*

The guidelines also make it clear that in all cases, in assessing the effects of a merger, the Commission will consider both the possible anti-competitive effects arising from the merger and the pro-competitive effects stemming from efficiencies identified and substantiated by the parties.

Finally, there is another clarification in the introductory part that it is worth mentioning. The guidelines indicate that when intermediate customers are actual or potential competitors of the parties to the merger, the Commission will focus on the effects of the merger on the customers to which the merged entity and those competitors are selling. Consequently, the fact that a merger affects competitors is not in and of itself viewed as a problem. It is the impact on effective competition on which the Commission will focus, not the mere impact on competitors at some level of the supply chain.

1. Definition of "Safe Harbours"

One important objective of the guidelines is to enable firms to identify easily those mergers that are unlikely to be challenged on competition grounds. To this purpose, the guidelines include a number of thresholds ("safe harbours"), expressed both in qualitative and quantitative terms, and indicate that it is unlikely that the Commission would identify competition concerns with regard to mergers falling below such thresholds.

First of all, the draft guidelines stated that non-horizontal mergers pose no threat to effective competition unless the merged entity has market power in at least one of the markets concerned.⁶⁹ Many respondents to the public consultation argued, however, that the notion of "market power" was too wide and not clearly defined by case law. Some would prefer to qualify it (and refer to "substantial" or "significant" market powers) and some argued that dominance, rather than market power should be the benchmark. In the final text of the guidelines the Commission took these comments into account; they now state that "non-horizontal mergers pose no threat to effective competition unless the merged entity has a significant degree of market power (which does not necessarily amount to dominance) in at least one of the markets concerned."⁷⁰

69. See Draft Guidelines, *supra* note 48, ¶ 23.

70. See Guidelines, *supra* note 4, ¶ 23.

The guidelines also include numerical “safe harbours” as a screen to identify cases that are unlikely to raise competition issues. The guidelines provide that the Commission is unlikely to find concerns in relation to non-horizontal mergers where the market share post-merger of the new entity in each of the markets concerned is below thirty percent⁷¹ and where the post-merger Herfindahl-Hirschman-Index (“HHI”) is below 2000.⁷² In practice, it will not extensively investigate such mergers, except where some special circumstances are present, which render market shares less useful as a proxy for the competitive conditions in the market.

It must be noted that a number of respondents to the public consultation on the draft guidelines criticized these safe harbours as overly cautious. In particular, it was mentioned that thirty percent represents only five percent more than the threshold used in the Form CO to identify vertically affected markets. It was also indicated that the threshold to be used for merger assessment should be higher than the one applying to vertical agreements, in particular in view of the efficiencies that normally derive from the former. A threshold of forty percent appeared to be the preference of several commentators. A few also suggested that an additional safe harbour could be introduced referring to the presence of the merged entity, not only in the foreclosing market, as it is the case now, but also in the foreclosed one. The Commission, however, did not take these comments on board and maintained the same quantitative thresholds in the final guidelines as in the published draft.

2. Assessment of Vertical Mergers

a. Non-Coordinated Effects: Foreclosure

With regard to vertical mergers, the guidelines identify two principal foreclosure scenarios: input foreclosure and customer foreclosure.⁷³ The first takes place when the merger is likely to raise the costs of downstream rivals by restricting their access to an important input.⁷⁴ The second takes place when the merger

71. *See id.* ¶ 25; *see also* Commission Regulation No. 2790/1999, O.J. L 336/21 (1999).

72. *See* Guidelines, *supra* note 4, ¶ 25.

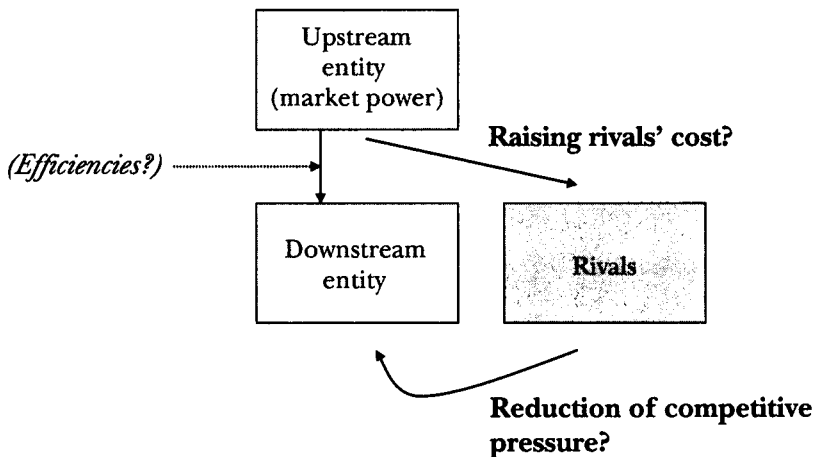
73. *See id.* ¶ 30.

74. *See id.*

is likely to foreclose upstream rivals by restricting their access to a sufficient customer base.⁷⁵

b. Input Foreclosure

A merger may significantly impede effective competition through input foreclosure where, post-merger, the new entity would be likely to restrict access to the products or services that it would have otherwise supplied absent the merger, thereby raising its downstream rivals' costs by making it harder for them to obtain supplies of the input at similar prices and under similar conditions as they could have absent the merger. This may give the merged entity the ability and the incentive profitably to increase the price charged to consumers. Any efficiencies resulting from the merger, however, may lead the merged entity to reduce price, so that the overall likely impact on consumers may be neutral or positive. The figure below gives a graphical presentation of this mechanism:⁷⁶



➡ Overall effect on consumers?

The guidelines outline a variety of factors that may in practice affect a merged firm's ability and incentive to foreclose, and the extent of any impact on consumers. For example, a foreclo-

75. *See id.*

76. *Id.* ¶ 31.

sure strategy can be effective only if the merged firm has a significant degree of market power in the input market⁷⁷ and the input represents a significant cost factor or an otherwise critical component for rival firms.⁷⁸ Incentives to foreclose are affected, among other factors, by the trade-off the merged firm has to make between the profit lost in the upstream market due to a reduction of input sales to (actual or potential) rivals and the profit gain from expanding sales downstream or, as the case may be, being able to raise price in that market.⁷⁹

In relation to legal disincentives, the guidelines start by quoting the jurisprudence of the Court, and by stating that when the adoption of a specific course of conduct by the merged entity is an essential step in foreclosure, the Commission will examine both the incentives to adopt such conduct and the factors liable to reduce, or even eliminate, those incentives, including the possibility that the conduct would be unlawful. It is also indicated that this appraisal, however, does not require an exhaustive and detailed examination of the rules of the various legal orders which might be applicable and of the enforcement policy practiced within them. But the guidelines try at the same time to provide some guidance as to which factors will be taken into account by the Commission in proceeding with such an analysis. They indicate that such factors will be, in particular: (i) the likelihood that this conduct would be clearly, or highly probably, unlawful under Community law, (ii) the likelihood that this illegal conduct could be detected, and (iii) the penalties which could be imposed.⁸⁰

Further, the guidelines deal with the effects of the merger on effective competition. To this regard, it is normally required that the foreclosed firms play a sufficiently important role in the competitive process on the downstream market.⁸¹ However, in certain circumstances, effective competition may also be significantly impeded by raising barriers to entry to potential competitors.⁸²

The guidelines also make it clear that the effect of the

77. *See id.* ¶ 35.

78. *See id.* ¶ 34.

79. *See id.* ¶ 40.

80. *See id.* ¶ 46.

81. *See id.* ¶ 48.

82. *See id.* ¶ 49.

merger on competition needs to be assessed in light of any efficiencies identified and substantiated by the merging parties. For the Commission to take account of efficiency claims in its assessment of the merger, the efficiencies have to benefit consumers, be merger-specific and be verifiable.⁸³

The section on efficiencies attracted substantial interest in the public consultation. A number of replies criticized the fact that the draft guidelines applied the same burden of proof for efficiencies as the Horizontal Merger Guidelines. It was argued that efficiencies are an inherent part of non-horizontal mergers and that the burden of proof should therefore be lower. A number of respondents would also like more detailed guidance on how the Commission will balance anti-competitive effects and efficiencies in these cases. Some also requested further clarification that the Commission will not apply an "efficiency offence" doctrine. The Commission reacted to these comments by clarifying some aspects of the section on efficiencies and provided an explicit response to the "efficiency offence" claim, by clearly indicating in the final guidelines that "the fact that rivals may be harmed because a merger creates efficiencies cannot in itself give rise to competition concerns."⁸⁴

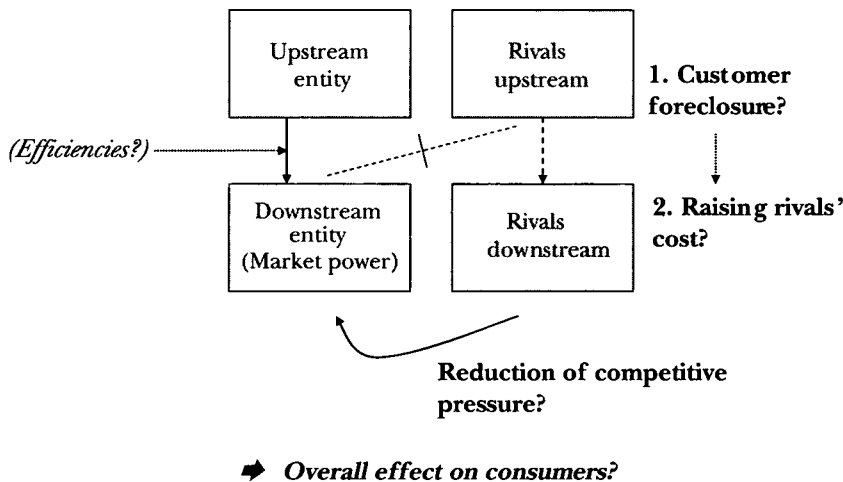
c. Customer Foreclosure

Customer foreclosure may occur when a supplier integrates with an important customer in the downstream market. Because of this downstream presence, the merged entity may foreclose access to a sufficient customer base to its actual or potential rivals in the upstream market (the input market) and thereby reduce their ability or incentive to compete. In turn, this may raise downstream rivals' costs by making it harder for them to obtain supplies of the input at similar prices and under similar conditions as they would absent the merger. This may allow the merged entity profitably to set higher prices in the downstream market. Again, any efficiencies resulting from the merger may lead the merged entity to reduce price, so that there is no overall negative impact on consumers. Like for input foreclosure, the Commission's assessment will include an analysis of the merged

83. *See id.* ¶¶ 52-57. On this point, the guidelines refer to the paragraphs on the assessment of efficiencies included in the horizontal guidelines.

84. *Id.* ¶ 16.

firm's ability and incentive to engage in a foreclosure strategy, as well as an evaluation of the potential size of the detrimental impact on consumers. A graphical representation of this mechanism is provided in the figure below:⁸⁵



d. Coordinated Effects

The guidelines provide an overview of factors that typically enhance firms' ability to effectively co-ordinate their competitive behavior. The section is based on the requirements set out by the CFI in the *Airtours PLC v. Commission* judgment.⁸⁶ Three conditions are, thus, necessary for coordination to be sustainable. First, the coordinating firms must be able to monitor to a sufficient degree whether the terms of coordination are being adhered to. Second, discipline requires that there is some form of credible deterrent mechanism that can be activated if deviation is detected. Third, the reactions of outsiders, such as current and future competitors not participating in the coordination, as well as customers, should not be able to jeopardize the results expected from the coordination.

3. Assessment of Conglomerate Mergers

The final sections of the guidelines are dedicated to con-

85. *See id.* ¶ 58.

86. *Airtours PLC v. Commission*, Case T-342/99, [2002] E.C.R. II-2585.

glomerate mergers.⁸⁷ These are mergers between firms that are in a relationship which is neither purely horizontal (as competitors in the same relevant market) nor vertical (as supplier and customer). In practice, the focus is on mergers between companies that are active in closely related markets (e.g. mergers involving suppliers of complementary products or of products which belong to a range of products that is generally purchased by the same set of customers for the same end use).

While the guidelines acknowledge that conglomerate mergers will, in most circumstances, not lead to any competition problems, they try to identify those specific cases where there may be harm to competition. The section on conglomerate mergers follows essentially the same structure as the guidance on vertical mergers.⁸⁸ The draft distinguishes between non-coordinated effects (foreclosure) and coordinated effects as principal theories of harm.⁸⁹ Foreclosure through tying and bundling are the principal potential theories of harm discussed in the section. The guidelines downplay the so-called "portfolio effects" theories in the absence of tying or bundling, and do not make any reference to possible theories based on the financial strength of one or more of the merging parties.⁹⁰

The guidelines outline the factors that may give a merged firm the ability and the incentive to foreclose (conceptually, the analysis is similar to the one proposed for consumer foreclosure theories) and presents the parameters affecting the likely overall impact of a conglomerate merger on prices and consumer choice. The guidelines also discuss potential sources of efficiency gains in this context, including pricing efficiencies ("Cournot effect").⁹¹

IV. *THE COMMISSION'S RECENT ENFORCEMENT PRACTICE*

In recent years the Commission has assessed an important number of mergers involving non-horizontal aspects. While most of these operations did not raise competition concerns, there were a few of them that required a closer investigation, or

87. See Guidelines, *supra* note 4, ¶ 91.

88. See *id.* ¶ 28.

89. See *id.* ¶¶ 91-118.

90. See *id.* ¶ 104.

91. See *id.* ¶¶ 115-18.

even remedial action, to eliminate possible non-horizontal concerns.

Since the entry into force of the new Merger Regulation (on May 1, 2004) until the publication of the draft guidelines, there had been twelve cases where the Commission identified concerns after a second phase investigation. Out of these twelve cases, seven (fifty-eight percent) were based on purely horizontal grounds, four (thirty-three percent) included both horizontal and non-horizontal elements, and in one case (nine percent) the problem identified was of a purely vertical nature.⁹² As is evident from these statistics, non-horizontal mergers have represented a more limited source of concern, relative to horizontal ones, particularly in recent years, but certainly not an inconsequential one.

A. *Recent Vertical Mergers Analyzed by the Commission*

Three relatively recent vertical merger cases analyzed by DG Competition are presented in this section. They have been selected because they shed light on how the Commission's approach to vertical mergers, set out in the draft guidelines, works in practice, and in particular on its assessment of whether there is a risk of input or customer foreclosure post-merger.

These cases include *Philips/Intermagetics*,⁹³ which was cleared in first phase, *Thales/Finmeccanica/Alcatel Alenia Space and Telespazio (Thales)*,⁹⁴ which was cleared only after a second phase investigation and *ENI/EDP/GDP*,⁹⁵ which was prohibited. There are also a number of recent cases, not covered in this Article, where the Commission requested remedial action on the basis of vertical concerns.⁹⁶

92. If one would have examined, instead, the twenty prohibition decisions the Commission has adopted in merger cases since 1990, the following picture would emerge: twelve decisions (sixty percent) were based on purely horizontal grounds, six (thirty percent) were solely based on non-horizontal concerns and two (ten percent) included both horizontal and non-horizontal issues.

93. See, e.g., Pierre Lahbabi & Sophie Moonen, *A Closer Look at Vertical Mergers*, COMPETITION POL'Y NEWSLETTER, Summer 2007, at 11, 11-17, available at http://ec.europa.eu/comm/competition/publications/cpn/cpn2007_2.pdf.

94. Commission Decision No. COMP/M.4300, slip op. (Nov. 7, 2006), cited in O.J. C 123/10 (2006) (*Philips/Intermagetics*).

95. Commission Decision No. COMP/M.4403, slip op. (Apr. 4, 2007), cited in O.J. C 248/23 (2006) (*Thales/Finmeccanica/Alcatel Alenia Space & Telespazio*).

96. Commission Decision No. COMP/M.3440, slip op. (Dec. 9, 2004), cited in O.J. C 185/03 (2004) (*ENI/EDP/GDP*).

1. *Philips/Intermagnetics*

This case concerned the acquisition by Philips of Intermagnetics, its main supplier of magnets and radio frequency ("RF") coils. These are two key inputs for the magnetic resonance imaging ("MRI") systems developed and produced by Philips' healthcare systems division. The Commission examined whether Intermagnetics, once integrated in the Philips group, would have the ability and incentive to foreclose Philips' competitors on the downstream market for MRI systems, such as General Electric and Siemens.

With regard to magnets, the Commission did not identify concerns. Pre-merger, Intermagnetics had already been supplying ninety-ninety percent of its production of magnets to Philips for several years and major competitors were already vertically integrated. Vertical integration in this area would rather facilitate cooperation in product development and provide Philips with the security of sourcing of its own magnets in the future.

With regard to RF coils, however, the situation was different. Intermagnetics held high market shares on the open market, and pre-merger it supplied this key input to several third party MRI manufacturers. In view of this, the Commission analyzed in detail the ability and incentives of the merged entity to engage in input foreclosure.

The ability of the new entity to foreclose RF coils customers proved to be limited for several reasons. In the short term, the merged entity would be bound by existing RF coil supply contracts linking Intermagnetics to its customers. These were long-term contracts with severe penalty clauses for any disruption of supply, and a close analysis of these contracts showed that they would have made a scenario of voluntary disruption post-merger counter-productive.

In the longer term, any attempt by the merged entity to disrupt supply to existing customers by Intermagnetics could be faced by counter-strategies by these customers. The market investigation showed that customers could turn to at least one other RF coil manufacturer that was deemed able to step up its production of RF coils. Furthermore, the customers in question had the strong research capabilities and the expertise necessary to develop and manufacture RF coils and would be able to produce a new model of RF coils within two years. As a matter of

fact, there had been several instances in the past of such customers switching from RF coil supply by Intermagnetics to internal production in less than two years. Alternatively, Intermagnetics's customers would be able to sponsor entry upstream, in particular by RF coil suppliers that could turn to the supply of RF coils for MRI systems relatively quickly.

It is worth noting that, in assessing counter-strategies, the Commission took a pro-active view, taking into account possible alternatives for Philips's rivals, such as developing their internal capabilities or sponsoring entry by a new supplier, that would only have medium term effects.

The Commission also concluded that the incentives for the new entity to engage in any form of input foreclosure after the expiration of the supply contracts were minimal. It appeared that the new entity could not expect to make profits by refusing to supply RF coils.⁹⁷ Philips made low gross and incremental margins on the market for MRI systems. However, relative to Philips' MRI activity, the RF coil activity of Intermagnetics was very profitable. Thus, refusing to supply RF coils would require substantial expected extra sales of MRI systems to offset the loss of RF coil sales. Neither did input foreclosure by means of price increases seem to be a profitable avenue for the merged entity.⁹⁸ RF coils account for a relatively limited percentage of the MRI costs. The Commission assessed what impact a substantial increase in the price of coils might have on GE's and Siemens's cost structure and concluded that they would not be likely to force them to increase their selling prices of MRI on a sustainable basis, in particular in view of their ability to switch or develop alternatives in the medium term.

Analysis of incentives of the kind carried out in this case was rarely found in the Commission's decisions before the *Tetra/Sidel* judgment. However, it has now become commonplace in any assessment of possible anti-competitive effects resulting from

97. See, e.g., Commission Decision No. COMP/M.4494, slip op. (Feb. 20, 2007), cited in O.J. C 5/4 (2007) (Evraz/Highveld); Commission Decision No. COMP/M.4314, slip op. (Dec. 11, 2006), cited in O.J. C 258/25 (2006) (Johnson & Johnson/Pfizer Consumer Healthcare); Commission Decision No. COMP/M.3696, slip op. (Dec. 21, 2005), cited in O.J. C 140/5 (2005) (E.ON/MOL).

98. Or engaging in a disruption of supply that would compel customers to stop purchasing RF coils from Intermagnetics. See Philips/Intermagnetics, slip op, *supra* note 94, ¶¶ 56-57.

non-horizontal mergers. In some instances, the costs and profits of different foreclosure strategies can be quantified and compared while in others, where such quantification will not be possible, the Commission will rely on proxies and reliable indicators, as provided for in the draft guidelines. The most detailed and sophisticated analysis of such incentives to date in a Commission decision is probably to be found in the *Thales/Finmeccanica/Alcatel Alenia Space & Telespazio* decision.

2. *Thales/Finmeccanica/Alcatel Alenia Space and Telespazio*

This case concerned the acquisition by Thales of Alcatel's holdings in Alcatel Alenia Space ("AAS") and Telespazio, two joint ventures jointly controlled pre-merger by Alcatel and Finmeccanica, respectively active in space systems and space services. The evidence collected during the first phase investigation pointed to serious competition concerns, essentially in the form of possible input foreclosure. Moreover, the package of behavioral commitments offered by the parties were, in the Commission's analysis, insufficient to remove these concerns in a clear-cut manner. The in-depth investigation, however, removed the Commission's serious doubts as to the compatibility of the proposed transaction with the Merger Regulation, and it was ultimately cleared without conditions.

The notified operation involved a three-level vertical integration. At the upstream level, the operation combined Thales's activities as a producer of Travelling Wave Tubes ("TWTs"), a key component of commercial telecommunications satellites, and AAS's activities in the field of Electronic Power Conditioners ("EPC"), another essential satellite component. Combined with TWTs, EPCs constitute the Travelling Wave Tube Amplifiers ("TWTAs") that are used to amplify the satellite's electro-magnetic signals before they are sent back to Earth. TWTAs, therefore, represented the intermediate level of vertical integration. Finally, at the downstream level, AAS operated as a commercial telecommunications satellite prime contractor.

Given the characteristics of the space industry, there are a very small number of market players at each level of the value chain. In particular, at the upstream level Thales has a very strong, almost dominant position in TWTs. L-3 Communications ("L-3"), a U.S. company, is its only competitor. Tesat (a subsidiary of EADS N.V.) and L-3 are the two leading players at

the upstream EPC and intermediate TWTA levels. The downstream market for commercial telecommunications satellites is more competitive, with two European players, AAS and Astrium (a subsidiary of EADS N.V.), four American suppliers (Boeing, Lockheed Martin, Loral and Orbital) as well as Russian, Chinese and Indian players.

In view of this market structure, the Commission examined the ability, likelihood and potential effect of input foreclosure at two levels—at the intermediate TWTA market and at the downstream satellite prime contracting level.

With regard to the examination of ability, a crucial issue was the competitive constraint exercised by L-3 on Thales for TWTs. Indeed, evaluating L-3's competitive strength was necessary to understand whether Thales's TWT customers would switch to L-3 if they were foreclosed. The in-depth investigation demonstrated that L-3 was a credible competitor to Thales for most TWT frequency bands and that the majority of TWT customers considered that L-3's TWTs were competitive as compared to Thales's. L-3 also has a major competitive advantage in that it is completely vertically-integrated and produces its EPCs internally. Due to this presence of L-3, the Commission considered that the merged entity would incur a significant commercial risk if it were to foreclose its downstream rivals, as it would lose TWT sales without being certain to gain a decisive advantage at the TWTA or satellite levels.

In assessing ability, it was also necessary to assess whether it would be feasible for the merged entity to combine AAS's EPCs with Thales's TWTs to foreclose its rivals. As regards EPCs, the market investigation established that Tesat and L-3 were the two leading players in terms of product range and production capacities and that AAS was not considered a credible supplier of EPCs by most market players. In particular, AAS does not have dual EPCs (EPCs that provide power to two TWTs), which account for half of the EPC demand. This is a growing market segment. The development, qualification and the acquisition of flight heritage of AAS's dual EPCs will require several years. AAS also has a limited EPC production capacity and would be unable to increase this capacity rapidly. In view of the above, it was concluded that the merged entity's ability to integrate AAS's EPCs with Thales's TWTs and foreclose its competitors was further restricted. Indeed, the merged entity would remain dependent on

third-party suppliers for at least half of its EPC needs and any attempt to foreclose them, and in particular Tesat, with regard to TWTs, could lead to retaliation on EPC supplies.

With regard to the assessment of incentives, as in *Philips/Intermagnetics*, the Commission evaluated Thales's and AAS's margins at each level of the supply chain. It turned out that, due to more intense competition, that margins are lower at the satellite level than at the component level. The different margins available at the different production levels, therefore, would not give Thales incentives to forego sales of profitable satellite components for uncertain benefits at the sub-systems or satellite level. Indeed, as seen before, it is not guaranteed that a TWT foreclosure strategy would increase significantly AAS's chances to win satellite bids since L-3 offers competitive TWTs. In addition, the overall competitiveness of satellite prime contractor offers depends not only on the TWTs but also on a broad range of parameters (satellite architecture, satellite subsystems, schedule and price, etc.). The benefits of any foreclosure strategy are therefore highly uncertain.

While these general considerations are valid for the most common TWTs and EPCs, the ability and incentives to foreclose might vary for certain specific combinations and depending on customer preferences. The particularly interesting element of this case is, precisely, that the Commission identified a number of market segments based on TWT, EPC and customer preferences, and assessed separately the new entity's ability and incentives to foreclose in each market segment. The relative importance of these market segments was estimated on the basis of all telecommunications satellites contracts awarded between 2001 and 2006. In this way, the Commission quantified the share of the TWT/EPC market on which foreclosure was likely. This analysis showed that foreclosure was likely only in less than ten percent of TWTA and satellite bids.

This decision is also interesting with regard to the assessment of legal disincentives. The Commission only examined foreclosure strategies that would have affected the rivals of the merged entity through non-price parameters. Indeed, these practices could not be detected by other market participants, or by antitrust enforcers, and therefore, even if they might be illegal, this illegality could not be considered a disincentive.

Finally, the Commission assessed the likely effects of the transaction. Given the very limited market segments where the new entity would be able to foreclose its rivals, these would not likely be marginalized or forced to exit the market. But even if an extreme scenario could be envisaged, where Tesat would be forced to exit the market, Thales would effectively replace Tesat and the current duopoly situation with L-3 would remain unchanged.⁹⁹ The transaction could also possibly be beneficial to competition if the new entity were to enter those narrow market segments, where it is currently not operating, in competition with Tesat and L-3. The new entity could emerge as a third player on certain segments of a market where there are only two players at present.

At the prime contracting level, the Commission assessed whether a foreclosure strategy limited to very narrow market segments would negatively affect the competitiveness of the merged entity's rival satellite prime contractors. This appears to be implausible since satellite prime contractors are generally active in several market segments and achieve a significant part of their business in the institutional market (with national and international space agencies), which is not affected by the proposed transaction. In addition, there are several credible prime contractors, which makes the market for commercial telecom satellites very competitive. This essentially excludes the risk of a significant impediment to competition.

The assessment of possible effects described in the previous paragraphs shows the clear emphasis that the Commission is placing on consumer welfare. Indeed, even the possible foreclosure of a particular competitor is not seen as grounds for intervention if the competitive outcome would not be worsened for customers one level below. The general principles described in the guidelines in this regard are clearly illustrated in this case.

3. ENI/EDP/GDP

The decision in the *ENI/EDP/GDP* case provides a good illustration of the various types of vertical effects that the Commission may identify. Although, in this specific case, it was found

99. *Id.* ¶ 62. As put forward in the Draft Guidelines, the lower the margins upstream, the lower the loss from restricting input sales. In this case, conversely, upstream margins were relatively high.

that each of these effects were likely to occur as a result of the merger, they remain conceptually independent from each other.

The planned merger concerned the proposed acquisition of Gás de Portugal ("GDP"), the incumbent gas company, by both Energias de Portugal ("EDP"), the incumbent electricity company, and Eni Spa ("ENI"), an Italian energy company. The merger was a vertical one to the extent that gas-fired power plants have now become, for economic and environmental reasons, the most common way of producing electricity. Gas is also an important input because it represents one of the main production costs of these plants (around seventy percent of the variable costs). Several markets were affected by the operation both within the electricity and the gas sectors, in which each of both EDP and GDP, as incumbents, respectively held dominant positions pre-merger.

With respect to electricity, the Commission first found that the merger would have given rise to several types of vertical anti-competitive effects on the downstream wholesale market. Having established that EDP's actual competitor would have no alternative for its gas supplies than GDP in the medium term, the Commission considered that the merger would have resulted in input foreclosure because EDP would have had both the ability and the incentives to raise its rival's costs, either by increasing its prices and/or by managing the constraints in gas supply to the detriment of the latter. The Commission also found that, by gaining *access to sensitive information* relating to its competitor's main input costs and daily nominations, EDP would have gained increased market power. Indeed, given the specific features of the market, in which its competitor's plant was next in the merit order, such information would have allowed EDP to increase its prices to the level of its competitor's with no fear of losing sales, to the detriment of customers. For those reasons, the Commission further considered that the merger would have foreclosed potential *entry*, if any, since future power generators would have had to be supplied, under the same conditions, by their main competitor. In addition, the Commission found that the merger would have given rise to significant horizontal anti-competitive effects by removing GDP as the best-placed potential competitor on the various electricity markets concerned (i.e. wholesale, retail and balancing power markets). For all these reasons, considered independently, the Commission concluded that EDP's

dominant positions on the downstream electricity markets would have been strengthened as a result of the merger.

On the upstream gas markets, the Commission found that the merger would have foreclosed all gas demand (customer foreclosure) on the distinct markets for gas supply to gas-fired power plants and to local distribution companies, which could otherwise have been challenged by potential competitors of GDP, once those markets are open to competition. This was mainly due to the fact that EDP would have been a significant challengeable customer absent the merger, access to which was essential for a potential entrant to reach the minimum efficiency scale to be able to operate viably. The Commission determined that, post-merger, EDP's incentives would have been to get supplies from its subsidiary GDP, rather than to solicit tenders from potential entrants. Accordingly, GDP's dominant position would have been strengthened. In the various electricity retail markets, the Commission's competition concerns were based on the horizontal effects that the merger would have caused, by removing EDP as the most likely entrant.

This decision was also interesting with regard to the issue of legal disincentives. The parties argued, in effect, that some of the foreclosure practices advanced by the Commission could be illegal, not only from the point of view of EU competition law but also with regard to national regulatory provisions. The Commission examined such claims, but concluded that a dominant operator in the gas wholesale market could use different mechanisms to degrade supply to its competitors downstream that could not be detected by national regulators in a timely fashion¹⁰⁰ and, therefore, would not face a disincentive to engage in such practices, even under the assumption that they might be considered illegal.

In the absence of adequate remedies for each of those competition concerns, the merger was declared incompatible with the common market. The decision was upheld by the CFI.¹⁰¹ The CFI, however, decided not to examine the Commission's assessment of the vertical effects of the merger as it found that its

100. See *Thales/Finmeccanica/Alcatel Alenia Space & Telespazio*, slip op. *supra* note 95, ¶ 343.

101. See *ENI/EDP/GDP*, slip op., *supra* note 96, ¶ 424; see also Commission Decision No. COMP/M.3696, slip op. ¶ 433, ¶¶ 443-46 (Dec. 12, 2005), cited in O.J. C 140/5 (2005) (E.ON/MOL).

horizontal effects (i.e. the loss of potential competition) were sufficient, in the absence of adequate remedies, to justify a finding of incompatibility.

B. *Recent Conglomerate Cases Assessed By the Commission*

Since the entry into force of the new Merger Regulation in May 2004, the Commission has not identified conglomerate concerns in a single case.¹⁰² There have been a few instances, however, where such concerns have been investigated before a clearance decision was finally adopted.

In this Section, two cases are described where the Commission recently examined possible conglomerate concerns. They include *GE/Amersham*¹⁰³ and *Procter & Gamble/Gillette*.¹⁰⁴ Both cases provide a good illustration of the steps that the Commission follows in such an assessment and the factors that matter in assessing in practice such potential concerns.

1. *GE/Amersham*

The case involved the acquisition by GE of the U.K. company Amersham, a producer of diagnostic pharmaceuticals. Diagnostic pharmaceuticals are complements to various types of diagnostic imaging equipment supplied by GE (in particular X-ray, CAT scan, ultrasound, magnetic resonance and nuclear imaging equipment). Both GE and Amersham had market leading positions in their respective areas of activity in certain EU Member States. As a result of the transaction, GE would be able to supply customers with complete diagnostic imaging solutions, including equipment and diagnostic pharmaceuticals.

The Commission investigated whether GE would have the ability and incentive to bundle or tie the two complements and whether such a strategy would negatively affect competition in

102. See EDP—Energias de Portugal, SA v. Commission, Case T-87/05, [2005] E.C.R. II-3745.

103. And since the prohibition of GE/Honeywell, the Commission has only adopted two decisions, both relating to the same medical equipment market, requiring remedial action on the basis of conglomerate concerns. See Commission Decision No. COMP/M.2861, slip op. (Apr. 30, 2003), cited in O.J. C 311/12 (2002) (Siemens/Dragerwerk/JV); Commission Decision No. 2004/322/EEC, O.J. L 109/1 (2003) (GE/Instrumentarium).

104. See Commission Decision No. COMP/M.3304, slip op. (Jan. 21, 2004), cited in O.J. C 301/10 (2003) (GE/Amersham).

the market for the supply of diagnostic imaging equipment and diagnostic pharmaceuticals to hospitals. Scenarios involving mixed bundling, contractual tying and technical tying were considered separately in the decision.

The Commission's investigation into the possibility of the merged entity engaging in such practices found significant differences in the procurement procedures and supply chains for imaging equipment and diagnostic pharmaceuticals, as well as very different procurement timelines. For instance, diagnostic imaging equipment has a long lifecycle of a minimum of ten years, whereas diagnostic pharmaceuticals are purchased as consumable products. While not entirely excluding the possibility of the merged entity engaging in commercial bundling, these market characteristics were found to reduce the likelihood of any anticompetitive effects resulting from such a strategy. In addition, technical characteristics, rather than price, were found to be the crucial factors in hospitals' purchasing decisions. Customers had a strong preference for mix-and-match solutions of their preferred components, reducing the effectiveness of bundled offers. Despite GE and Amersham's strong positions in certain product markets, there existed a number of strong rivals in each market who could counter any bundling effects.

Given customers' preference for combining so-called "best-of-breed" products (as opposed to committing to a product bundle offered by a fixed supplier pair) and the existence of several unbundled alternatives, the Commission's investigation also rejected the possibility that GE/Amersham could engage in a contractual or technical tying strategy to the detriment of customers. On the basis of this analysis, the Commission cleared the transaction after a first-phase investigation.

2. *Procter & Gamble/Gillette*

Horizontal effects from the merging firms' overlapping activities in oral care and personal hygiene products were the primary focus of the Commission's investigation in the Procter & Gamble/Gillette case. However, the Commission also considered possible conglomerate effects, arising from the fact that some of the parties' products were complements (e.g. toothbrushes and toothpaste) and, more generally, that retail chains purchase a wide range of their products simultaneously. The

Commission's investigation focused on the possibility of foreclosure resulting from the bundling of different products, as well as on possible anticompetitive effects related to the merging firms' position as so-called "category manager".

As to bundling, the Commission examined, in particular, whether the merger would enable P&G and Gillette to impose weak brands on their customers, to foreclose competitors from access to the retailers' limited shelf space or to hinder entry of new products to the market through tying or bundling practices. However, a number of factors, including the presence of several strong competitors, often with similarly wide product ranges, and retailers' buyer power, led the Commission to conclude that competitive harm was unlikely. The merger's competitive impact was also limited by the fact that potential bundling opportunities arise mainly within product categories (e.g. wash powder and softener) rather than across categories (e.g. feminine care and male wet shaving).

The Commission noted, in particular, that Procter & Gamble/Gillette's enlarged product range may lead to efficiencies from one-stop-shopping and economies of scope (e.g. in logistics). In view of the fact that no likelihood of foreclosure had been identified, there was no need for the Commission to attempt to quantify such efficiencies and/or balance them against possible anti-competitive effects. However, the recognition that specific efficiencies may arise from extended product ranges clearly shows the Commission's willingness to take these positively into account in the assessment of non-horizontal mergers. This statement could also be seen as pointing towards a more sceptical attitude with regard to theories of harm based exclusively on portfolio effects, at least in the absence of foreclosing practices such as bundling or tying.

The Commission approved the transaction after a first-phase investigation subject to divestiture commitments removing horizontal competition concerns.

CONCLUSION

This brief overview of recent cases involving the assessment of vertical and conglomerate effects demonstrates that the Commission has integrated in its practice the sound principles established by the recent jurisprudence and developed a consistent

approach and methodology to assess the impact on competition of non-horizontal mergers.

In particular, it illustrates how the three-step analysis which was elaborated in the Courts' jurisprudence and which has become the basis for the analytical framework in the Non-Horizontal Merger Guidelines, works in practice. The need for the Commission to assess (i) the merging parties' ability to foreclose, and (ii) their incentives to pursue a foreclosure strategy, followed by (iii) an analysis of the impact that such foreclosure would have on consumers in the downstream markets, imposes a welcomed rigour in the Commission decisions' reasoning, limiting enforcement intervention to cases where consumer harm appears likely.

These cases also demonstrate that, in assessing non-horizontal operations, the Commission fully examines the elements that can point towards the ability of the merged entity to foreclose, but also those reducing the likelihood of foreclosure, including possible counter-strategies that might be pursued by its rivals post-merger. If ability cannot be excluded, incentives are systematically assessed, in line with the approach adopted by the CFI in the *GE/Honeywell* judgment. As the Commission's decision in *Thales/AAS* illustrates, this analysis has already reached considerable levels of sophistication in some cases.

The examination of legal disincentives also appears now to be well integrated in the Commission's practice, despite the not always consistent guidance provided on this issue by the courts. It is noteworthy that merging parties are now frequently pointing to the existence of such a disincentive, at least to the extent that dominance can be easily established or when national regulatory regimes would apply to the merged entity. The Commission, however, is dealing with such claims realistically: it may conclude, for example, that clearly illegal and easily detectable foreclosing practices should not be taken into consideration, but in many instances, as seen in *ENI/EDP/GDP*, the merged entities have other alternative means of foreclosing rivals, which may be considerably more difficult to detect and punish, and which should therefore be taken into account in the analysis.

The cases examined also highlight the focus on consumer welfare as the ultimate goal of EU merger control. In *Philips/Intermagnetics*, in spite of high market shares upstream in the "open" market, vertical concerns were excluded because no

harm to downstream customers could be shown. Similarly, in *Thales/AAS*, a detailed analysis of the competitive constraints on the merging parties allowed the Commission to discount possible competition concerns arising from the high levels of concentration at various stages of the value chain. The Commission ended up clearing an operation, despite some risk of foreclosure of a competitor, because the likelihood of consumer harm could not be established.

Finally, the cases examined above did not require the Commission to balance anti-competitive effects and efficiencies, even if efficiencies arising from an extended product range were acknowledged in *Procter & Gamble/Gillette*. Such a balancing is likely to be one of the most difficult and controversial aspects of future assessments. Experience will tell whether the Commission is able to carry this out satisfactorily. The difficulty inherent in such analysis, however, should not in itself be a reason to refrain from engaging in the assessment of possible non-horizontal anti-competitive effects, as some have argued, in particular when recent practice shows that harm is likely to arise in certain scenarios where efficiencies would be unlikely to materialize.

The public consultation on the draft enforcement guidelines shows that this general approach was broadly welcomed and encouraged the Commission to adopt it definitively. This is what the final version of the guidelines did, after taking into account some of the comments received. It is now the duty of the Commission and the Courts to develop this guidance in individual decisions and judgments to enhance even further the coherence and predictability of EU Merger Control policy with regard to non-horizontal operations.