An Analysis of the Vertical Mergers Before and After the Adoption of the Non-Horizontal Merger Guidelines[*]

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I. INTRODUCTION

The aim of this paper is to provide an evaluation on the assessment of vertical mergers before and after the adoption of non-horizontal merger guidelines. The focus will be the decisions of the Community Courts and the Commission before and after the guidelines.

After this introduction, the second section of this paper will cover the European jurisprudence prior to non horizontal merger guidelines. In this section, the definition of non-horizontal mergers alongside with the definition of horizontal mergers will be introduced. The main focus of this section will be the Commission's and Community Courts' assessments of vertical mergers and for this reason, different cases will be analysed under this section.

In the third section, Commission's stance after the adoption of the Non-horizontal Merger Guidelines will be analysed. In this section, the main focus will be on the guideline and the commission's implementation of the guideline to the case law.

The final section of this paper will give a brief summary of this paper alongside with a general analysis of the issue.

II. PRIOR TO NON-HORIZONTAL MERGER GUIDELINES

1. The definition of Non-Horizontal Merger and the analysis of possible effects on competition.

Horizontal mergers are the mergers between the actual or potential competitors.[1] Since horizontal mergers are mergers between companies on the same market, horizontal merger will definitely remove an existing competitor from the market. Therefore, the market power of the merged entity will be significantly greater than the market power of either party before

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[*] This paper was prepared by the Author for the *Mergers and Acquisitions* course as part of the LLM International
Commercial Law program at City University London during 2011-2012 academic year.

[1] Korah Valentine, An Introductory Guide to EC Competition Law and Practice, 9th edition Hart Publishing p.411

the merger.[2] However, the term 'non-horizontal merger' is used as a general term for both vertical and conglomerate mergers by the European Commission and those mergers are mergers between companies active in different markets. This type of merger does not impede competition instantly. Moreover, non-horizontal mergers can even lead to pro-competitive effects, given that the merger may for example eliminate double mark-ups and give rise to a decrease in transaction costs. Investments could also be better co-ordinated post-merger. As a result of non-horizontal mergers, the prices of goods and services offered by the merged entity often decrease. In addition to price efficiencies, non-horizontal mergers can also give rise to non-price efficiencies, for example, the creation of one-stop shopping for many customers. These are static efficiencies, but non-horizontal mergers also produce dynamic efficiencies such as emulated competition. Competitors might also undertake non-horizontal mergers to be as competitive as the new merged entity and as a result produce the same pro-competitive effects.[3]

2. European jurisprudence on non-horizontal mergers prior to non-horizontal merger guidelines

The adoption of non-horizontal Merger Guidelines reveals the commission's more economic approach to merger control. Undoubtedly, the aim is improving consumer welfare standard. For many years there was a lack of clarity about the Commission's practice in terms of vertical merger cases, and its conclusions in Tetra Laval/Sidel[4] and in GE/Honeywell[5] were reversed on appeal. [6] After the adoption of the guidelines which provide valuable guidance as to how the commission assesses mergers where the undertakings concerned are active on different relevant market, the commission examines the ability of the merged entity to foreclose rivals, incentive of merged entity to foreclose rivals and whether this strategy would have a harmful effect on competition.[7] However, before the adoption of the guidelines, since there was not any specific guideline regulating non-horizontal mergers, the decisions of the commission were changing. In some cases, commission concluded that just the ability of the merged entity to foreclose rivals were sufficient to block the merger, however, in some

[2] Andreas Weitbrecht and Ronan Flanagan 'The control of vertical and conglomerate mergers before and after Ge/Honeywell- the commission's draft guidelines for non-horizontal mergers' Bloomberg European business Law journal Vol. 1:294 p.294
[3] Parizel Audrey, 'The European Commission's new guidelines on non-horizontal mergers' [2008] International Trade Law & Regulation
[4] Case C-12/03 P *Commission v Tetra Laval BV* [2005] ECR I-987
[5] Case T-209/01 *Honeywell International Inc v Commission of European Communities [2005] ECR II-5527*
[6] Richard Whish, Competition Law (6th edn, 2009, Oxford University Press) p.865
[7] Ibid,

cases commission also examined the merged entity's incentive to foreclose rivals. Under this section, some of the important cases will be examined.

Skanska/Scancem

This case concerns the merger of Scancem, Sweden's largest producer and distributor of cement and construction materials, and Skanska, the producer of ready-mixed concrete, dry concrete and pre-cast concrete products. According to Commission the merged entity would have 80-90 % of the Swedish market for cement production, 40-50% of the Swedish market in ready mix concrete and up to 80 % of the Swedish market in other building materials.[8] Based on those figures, the Commission held that the merged entities would create a dominant position on the Swedish market for ready-mixed concrete. This stems partly from the horizontal overlaps between Skanska and Scancem, and the fact that their combined market share would be significantly higher than those of all competitors. It is also caused from the vertical effects of the concentration, which means that the competing ready-mix producers would be largely dependent on Skanska/Scancem for their supplies of the key raw material, cement, and also for sales of ready-mixed concrete to Skanska in its capacity as Sweden's largest construction company. Finally, it is not likely that potential competition would play any important role in the foreseeable future, or that the customers of the combined entity would be in a position to effectively neutralise its ability to act independently on the market.[9]

The significance of the case is that in the commission's decision it is not taken into consideration whether the parties have an economic incentive to raise rivals' costs. The commission's primary focus was on the merging parties' ability to raise rivals' costs. This is important because in order for a foreclosure strategy to be profitable, the revenues foregone by the merging parties upstream have to be satisfactorily counterbalanced by increased profits downstream.[10]

EDP/GDP

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[8] Alvaro Ramos, Tricia Mohan and Francesco Carloni, 'Evaluating Vertical Mergers Post Non-Horizontal Guideline: An Economics-Based Approach?' The Global Competition Law Centre Working Papers Series, GCLC Working Paper 03/09

[9] Case No IV/M.1157 - Skanska/Scancem [1998] Para 147

[10] Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings 2008/C 265/07 Para 40

This case concerns the merger between GDP (Gas de Portugal), the incumbent gas company in Portugal and EDP (Energias de Portugal) the incumbent electricity company in Portugal and ENI, an Italian energy company. After a comprehensively analysis, the commission decided that the deal would have strengthened EDP's dominant position, notably in the Portuguese electricity wholesale and retail markets, and GDP's dominant position in the various gas markets in Portugal, as a result of which effective competition would have been significantly impeded.[11] In this case, commission focused primarily on the ability of the merging entities to increase rivals' costs and paid less attention to their economic incentive to foreclose. Remedy proposals were submitted by the parties at different stages of the procedure however, the commission concluded that these commitments were insufficient to eliminate the various competition concerns and declared that the proposed concentration incompatible with the common market.[12] Even though EDP brought an action to annulment of the decision of the commission, the court dismissed the appeal and upheld the commission' decision.[13]

Neste/Ivo

This case concerns the merger between NESTE, active in oil, energy and chemical business, and IVO, the largest Finnish company in the energy sector. IVO's business activities consist of power and heat generation, power trading and electricity distribution and supply, operation and maintenance of power plants, energy measurement.[14] The Commission was concerned that since natural gas was an input for electricity production, the parties could use their strong position in the natural gas market to raise competing electricity manufacturers' costs.[15] However, there is only 10% of the electricity production in Finland uses natural gas and therefore the economic incentive to raise rivals costs was quite small. However, the commission stated that 'natural gas is strategically very important for electricity production in Finland and that its importance will continue to increase over the next years.[16] It is clear that when the market share is high after a merger the parties should

[11] Case No COMP/M.3440 ENI / EDP / GDP [2004] Para 609
[12] Giuseppe CONTE, Guillaume LORIOT, François-Xavier ROUXEL and Walter TRETTON, 'EDP/ENI/GDP: the Commission prohibits a merger between gas and electricity national incumbents' (2005) 1 http://ec.europa.eu/competition/publications/cpn/2005_1_84.pdf accessed 20 April 2012
[13] Case T-87/05
[14] Case No IV/M.931 - NESTE / IVO paras 2-3
[15] Ibid., para 47
[16] Ibid., paras 33-34

give adequate remedies to ensure that markets will work efficiently. [17] In light of the Commission's concerns in Neste/IVO regarding the vertical integration of Neste's dominant position in natural gas with IVO's dominant position in electricity production and sale, the parties agreed to decrease Neste's controlling shareholding in Gasum to a minority interest.[18]

Telia/Sonera

This case concerns the merger between Telia, the largest telecommunication and cable TV operator in Sweden and Sonera, the largest mobile telephony operator in Finland and the largest provider of long distance national and international network services.[19] In the case, commission concluded that without the benefit of any economic assessment, that Telia would have an incentive to distort competition to Sonera's advantage. It was clear that the commission instinctively assume that it would be rational for Telia to favour its subsidiary Sonera. This case is also cleared by the commission under some remedies. As it is clearly stated above, the commission did not only take the merged entity's ability into consideration, it also took merged entity's economic incentive into consideration.

Imperial Tobacco/Altadis

This case concerns the merger between Imperial Tobacco and Altadis, two manufacturers of cigarettes and tobacco products. This is the first case the commission pays significant attention to the economic analysis of the merged entity's incentive to foreclose. The commission considered the vertical effects raised by the merging parties' distribution activities and eventually concluded that the merged entity would not have ability to foreclose rivals. The commission apparently relied on the fact that there is alternative distribution channels existed. And commission also accepted the conclusion that 'a foreclosure strategy would be profitable for the merged entity only under very extreme conditions, namely a very big increase in sales that is extremely unlikely in a market whose size is relatively stable'.[20]

Tetra/Sidel

This case concerns the merger between Tetra Laval, active on the market for equipment and consumables used in the production of carton packaging for liquid food and

[17] Jari Hyvarinen, 'EU Competition Policy- A Small Country Perspective' (2002) <http://www.etla.fi/files/926_FES_02_1_eu_competition.pdf> accessed 24 April 2012
[18] David Went, 'The Acceptability of Remedies under the EC Merger Regulation: Structural Versus Behavioural' [2006] E.C.L.R. 455
[19] Case No COMP/M.2803 - TELIA / SONERA [2002] paras 3-4
[20] Case No COMP/M.4581 -IMPERIAL TOBACCO / ALTADIS [2007]

Sidel, leading producer of stretch blow moulding(SBM) machines that are used to produce another type of liquid food packaging made of plastic material PET(polyethylene terphtalate). The commission block the merger with the opinion that Tetra Laval would leverage its dominant position in carton packaging into the market for the machines used to blow PET bottles. This complicated chain of events would then lead to Sidel attaining a dominant position in the market for these machines.[21] The commission also stated that eliminating Sidel which is an important competitor of Tetra Laval could deprive Tetra Laval of the incentive to be more innovative and lowering the prices. Tetra Laval then successfully appealed the commission’s decision to the CFI. Then the commission in turn appealed the CFI judgment to the ECJ but the commission was unsuccessful and ECJ upheld the decision of CFI.[22]

GE/Honeywell

This case concerns the unsuccessful merger attempt between the General Electric and Honeywell. GE was in a dominant position on the world market for jet engines for large commercial aircraft and large regional aircraft. Honeywell was the leading supplier of avionics and non-avionics products, as well as of engines for corporate jets and of engine starters, a key component in the manufacturing of jet engines. The commission found that the merger would give rise to the creation or strengthening of dominant positions in three different ways which are simple horizontal overlaps, conglomerate effects and vertical effects. In commission’s decision it is stated that General Electric's existing dominant position on the market for large commercial jet aircraft engines would be strengthened on account of the vertical effects of the merger resulting from the integration of GE's activity as a manufacturer of those engines with Honeywell's activity as a manufacturer of starters for those engines.[23] The commission block the merger and General Electric unsuccessfully appealed it and CFI upheld commission’s decision.

As it is obviously seen from the above decisions, the stance of the commission was evolving and in the GE/Honeywell decision, the organizing principles for the assessment of non-horizontal mergers are created for the Commission. While in the Skansca/Scancem

[21] Andreas Weitbrecht and Ronan Flanagan ‘The control of vertical and conglomerate mergers before and after Ge/Honeywell- the commission’s draft guidelines for non-horizontal mergers’ Bloomberg European business Law journal Vol. 1:294 p.298

[22] EU bulletin,[2005] < http://www.hoganlovells.com/files/Publication/d27d5b3f-a1b9-48d6-bdff-93df01294400/Presentation/PublicationAttachment/3e83f68f-035f-44a6-a784-f0c8431f558e/1785_050317_EU%20Bulletin%20-Tetra%20Sidel%20Changes.pdf> accessed 17 April 2012

[23] James Killick, ‘The GE/Honeywell judgment - in reality another merger defeat for the Commission’ [2007] Case comments, European Competition Law review

decision, it is not taken into consideration whether the parties have an economic incentive to raise rivals' costs and commission just focused on the ability of the parties to raise rivals' costs, In Telia/Sonera and Imperial Tobacco/Altadis cases commission focused on the ability and the incentive of the Telia to distort competition to Sonera's advantage, in other words commission also considered merging entities' economic incentives to raise rivals' costs.

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'.[24] This approach is related to effects part of commissions assessment which will be further analysed deeply below.

In GE/Honeywell and Tetra/Sidel cases, the commission's merger control decisions were cancelled for lack of persuasive evidence showing that the merging entities had either the ability or the incentive to engage post-merger in the alleged anti-competitive practices. In GE/Honeywell, the CFI required that the commission present either direct evidence proving that the merging parties were likely to engage in the alleged anti-competitive conduct or an economic assessment demonstrating that the alleged behaviour would objectively have been in the merged entity's commercial interest.[25]

Assessment of foreclosure theories

In the GE/Honeywell judgement, the Court of First Instance develops the general principles established by the ECJ and sets out detailed the different steps in the assessment that the Commission should do, 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 denial to deal or bundling by the merged entity, were at the centre of the Commission's case. The CFI starts by recognizing that the anti-competitive effects alleged by the Commission would have only followed from the merger in so far as the merged entity had acted in a certain way after the merger. In those circumstances, the Commission had the burden to provide persuasive proof to support its conclusion that the

[24] Carles Esteva Mosso, 'Non-Horizontal Mergers: A European Perspective' (2007) Fordham International Law Journal Volume 31, Issue 5 Article 12

[25] Alvaro Ramos, Tricia Mohan and Francesco Carloni, 'Evaluating Vertical Mergers Post Non-Horizontal Guideline: An Economics-Based Approach?' The Global Competition Law Centre Working Papers Series, GCLC Working Paper 03/09

merged entity would possibly behave in the way anticipated. This would require two aspects, firstly the Commission proves the capacity or ability to engage in such practices and secondly it would prove that it was likely for the merged entity to engage in such conduct. Once ability and likelihood have been established, the Commission is need to establish that those practices would have created or strengthened a dominant position on some of the markets concerned. [26]

i. Ability

It is clear that there are some conditions for a merged entity to be able to engage in foreclosure practices. In the GE/Honeywell judgment, the CFI mostly 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. Firstly, the CFI analyzes whether the market characteristics and the behaviour of customers would allow the merged entity to engage in those practices. And secondly, the CFI examine whether the Commission had established that the merged entity would have adequate market power in one of the bundled product markets so as to be able to impose the bundle profitably on customers.[27]

ii. The likelihood of foreclosure practices

According to CFI, documents showing the tendency of the board of directors of one of the merging parties to engage in certain practices after the merger could be deemed as persuasive proof showing that the likelihood of such practices taking place.[28] However, the likelihood of certain anti-competitive practices taking place mostly will depend upon the economic incentives that the merged entity will have to engage in them. Such incentives can be measured by comparing the likely costs to the merged entity of such practices with the benefits that they would be likely to make. In view of this, economic studies assessing such tradeoffs are often considered by the CFI as an essential means to convincingly show likelihood.[29]In other words, evidence of past conduct may not be enough to establish the legal standard that the merged entity would engage in certain conduct in the future and to establish

[26] Case T-210/01 *General Electric Company v Commission of the European Communities* [2005] paras 68-69-295-327-405

[27] Carles Esteva Mosso, 'Non-Horizontal Mergers: A European Perspective' (2007) Fordham International Law Journal Volume 31, Issue 5 Article 12

[28] Case T-210/01 *General Electric Company v Commission of the European Communities* [2005] paras 332-333 and 439-443

[29] Carles Esteva Mosso, see above note 27

the ability and the incentive to behave in a given way the Commission may rely upon the merged entity's commercial interest and logic.[30]

iii. Effects

It is obvious that the commission should also show that such foreclosure would give rise to some anti-competitive effects rather than confining itself to establishing the ability and likelihood of foreclosure theories. Without any doubt, the Merger regulation is based on a consumer welfare standard. Thus, it is not enough to prove incompatibility that some of the competitors are expelled in a certain market. Rather, it should be showed that, by increasing the costs of one or more competitors, or excluding them from the market, the merger would eventually have an anticompetitive effect and most significantly harm the consumer welfare.[31]

As it is stated in the GE/Honeywell judgment, anticompetitive effects are also needed to be proved, however, since 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 is not needed to analyses the commission's assessment of the effects.[32]

Even though, this case is considered as a victory of the commission, most of the authors and myself believe it is not a real victory since there are a lot of parts of the commission's decision were held illegal by the CFI, although it upheld Commission's decision. The most important outcome of this case is that the commission base its decision on rigorous economic study as well as on solid proof when it criticizes vertical effects.[33]

III. POST NON-HORIZONTAL MERGER GUIDELINES

After the abovementioned decisions of Community courts, the Commission published the guidelines on the assessment of non-horizontal mergers which adopted a more economically rigorous approach to its assessment of vertical mergers. However, it has to be emphasised that publication of the Non-horizontal merger guidelines had a little effect on the

[30] Matteo F Bay and Javier Ruiz, GE appeal ruling raises bar for merger control [2006] <http://www.lw.com/upload/pubContent/_pdf/pub1494_1.pdf> accessed 23 April 2012
[31] Carles Esteva Mosso, 'Non-Horizontal Mergers: A European Perspective' (2007) Fordham International Law Journal Volume 31, Issue 5 Article 12
[32] Case T-210/01 *General Electric Company v Commission of the European Communities* [2005] para 362
[33] Frank Romano, 'General Electric/Honeywell victory of the commission… or failure?' [2007] IBLJ

Commission's approach, because the Notice articulated the more economically rigorous approach that, by 2007, the commission was already applying in practice.[34]

According to Guidelines there are three possible concerns can arise from a vertical merger which are input foreclosure, customer foreclosure and access to confidential information. Input foreclosure takes place when the merger is likely to raise the costs of downstream rivals by restricting their access to an important input and customer foreclosure takes place when the merger is likely to foreclose upstream rivals by restricting their access to a sufficient customer base and the last concern arises when the merged entity able to gain access to confidential information on its rivals and ultimately reduce competition.

1. INPUT FORECLOSURE

According to guidelines input foreclosure arises 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 under similar prices and conditions as absent the merger. This may lead the merged entity to profitably increase the price charged to consumers, resulting in a significant impediment to effective competition.[35] And the guideline furthermore shows that there is a six stage analysis for assessing input foreclosure issues.

First step of assessing input foreclosure is identifying the leveraging conduct, second step is analysing whether the merged group will have the ability to pursue the leveraging conduct, third step is analysing whether the merged group will have the incentive to pursue the leveraging conduct, fourth step is identifying the foreclosure effect, if any, arising from the leveraging conduct, fifth step is assessing whether there is a causal link between the merger and any foreclosure effect; and last step is considering any efficiencies arising from the merger.[36]

a. Identify the leveraging conduct;

[34] Alistair Lindsay and Alison Berridge, EC Merger Control: Substantive issues (3rd edn, Sweet & Maxwell 2009) 402
[35] Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings 2008/C 265/07, para 31
[36] Ibid., paras 31-57

The first step of analysing input foreclosure issues is to identify the behaviour which the merged group might adopt in order to exclude or marginalise competitors. The notice identifies five main strategies: which are refusal to supply, restriction of supply, increase in price, choosing technology which is incompatible with that of downstream rivals, and lastly degrading the quality of the input supplied.[37]

b. Analyse whether the merged group will have the ability to pursue the leveraging conduct

The Commission has identified three necessary elements for a practicable foreclosure strategy. Firstly, the input should be an important input for the downstream production, secondly, the merged group must have a significant degree of market power in the upstream market[38], and lastly, there should not be any effective and timely counter strategies that rival firms would be likely to deploy.[39]

In Itema/BarcoVision decision, the Commission concluded that the merged entity will have a significant degree of market power upstream, and no alternative sources of sensors supplies in the short term are available, which speaks in favour of the ability to foreclose.[40]

In its Nokia/NAVTEQ decision in 2008, the Commission concluded that the merged entity would enjoy a significant degree of market power upstream as TeleAtlas was the only other provider of navigable digital map databases with a similar coverage and quality. However, the Commission concluded that it was uncertain whether the merged entity would have the ability to engage in input foreclosure as it was not clear whether navigable digital map databases are a significant input in the market for mobile handsets. In this regard, the Commission noted that digital maps only account for a relatively limited proportion of the cost of handsets with navigation functionality, approximately 0-15 per cent, although it also recognized that navigable digital map databases constitute a component without which navigation services could not be proposed on mobile handsets.[41]

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[37] Alistair Lindsay and Alison Berridge, EC Merger Control: Substantive issues (3rd edn, Sweet & Maxwell 2009) 409

[38] Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings 2008/C 265/07, paras 34-35

[39] Ibid., para 39

[40] Case No COMP/M.4874 – ITEMA / BARCOVISION[2008] para 70

[41] Mat Hughes and David Wirth, 'The Assessment of Non-Horizontal Mergers Under EC and UK Merger Control' (2010) ICLG to: Merger Control <http://www.iclg.co.uk/khadmin/Publications/pdf/3237.pdf> accessed 12 April 2012

In assessing the ability to engage in input foreclosure, historical buying patterns, existing supply arrangements and past changes in capacity in the upstream markets will often provide valuable information as to how customers and suppliers have previously responded to changes in the input prices of different suppliers, as well as providing an indication of the viability of switching to alternative suppliers or products post merger. In addition, case studies of recent capacity additions and entry in the input market may well be revealing as they will supply a hint of the complexity of entry, the costs and risks linked to entry, the possible scale of entry, how new products are marketed and dispersed and so on.[42]

c. Analyse whether the merged group will have the incentive to pursue the leveraging conduct

An assessment of the merged groups' incentive to pursue the leveraging strategy requires a careful analysis of the impact on the merged group's profits in the upstream market and downstream market.[43] In the Commission's TomTom/Tele Atlas decision, the Commission states that the merged entity comfort with a trade-off between the profit lost in the upstream market because of a decrease of input sales and the profit gained on the downstream market by raising its rivals' costs. A profit incentive calculation will depend upon a number of factors, including; the type of strategic behaviour being considered ,the amount of revenue that would be foregone from upstream input sales if the merged entity was to act strategically and the additional profit that would be gained by the merged entity selling more at a higher price downstream due to its downstream rivals' being forced to increase their prices or otherwise being unable to compete as effectively as they did before the merger.[44]

d. Identify the foreclosure effect, if any, arising from the leveraging conduct,

In order to establish that a merger creates a vertical competition concerns justifying a prohibition decision or the acceptance of commitments, it is not enough solely to show that the merged group is likely to adopt an input foreclosure strategy. It is also necessary to prove

[42] Mat Hughes and David Wirth, 'The Assessment of Non-Horizontal Mergers Under EC and UK Merger Control' (2010) ICLG to: Merger Control <http://www.iclg.co.uk/khadmin/Publications/pdf/3237.pdf> accessed 12 April 2012

[43] Alistair Lindsay and Alison Berridge, EC Merger Control: Substantive issues (3rd edn, Sweet & Maxwell 2009) 417

[44] Mat Hughes and David Wirth, 'The Assessment of Non-Horizontal Mergers Under EC and UK Merger Control' (2010) ICLG to: Merger Control <http://www.iclg.co.uk/khadmin/Publications/pdf/3237.pdf> accessed 12 April 2012

that such a strategy would have significant effects on the downstream market and therefore on consumers.[45]

An input foreclosure strategy may lead changes in the competitive conditions in the downstream market by raising the costs of downstream rivals which play an important role in the competitive process[46], by causing the exit of an important competitor or by raising barriers to entry, especially in industries that are opening up to competition or are expected to do so in the near future.[47]

In Nokia/NAVTEQ decision, the Commission clearly stated that mobile handset producers would not easily be impacted by the concentration since the cost of digital maps only accounts for a minimal share of their costs and because Tele Atlas would compete against NAVTEQ to increase sales of maps. In addition, handset manufacturers and MNOs would have the option to source their digital maps and navigation software from Garmin, which is protected from price increases via its long term deal with NAVTEQ. It is also clear from the Commission's Nokia/NAVTEQ decision that the Commission will consider efficiencies at the effects stage of the foreclosure analysis.[48] In this regard, the Commission stated that the general impact of the proposed transaction will also be affected by the likely efficiencies that are brought about by the merger and substantiated by the parties. While there is a lack of anticompetitive effects irrespective of efficiencies, these efficiencies form part of the overall competitive assessment.[49]

e. Assess whether there is a causal link between the merger and any foreclosure effect;

There has to be a causal link between the merger and the foreclosure effect. In Aeroports de Paris/the Nuance Group, the commission rejected input foreclosure concerns because ADP already had the ability to increase its market share on the downstream market.[50]

f. Consider any efficiencies arising from the merger.

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[45] Alistair Lindsay and Alison Berridge, EC Merger Control: Substantive issues (3rd edn, Sweet & Maxwell 2009) p.423
[46] Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings 2008/C 265/07, para 48
[47] Ibid, para 49
[48] Mat Hughes and David Wirth, 'The Assessment of Non-Horizontal Mergers Under EC and UK Merger Control' (2010) ICLG to: Merger Control <http://www.iclg.co.uk/khadmin/Publications/pdf/3237.pdf> accessed 12 April 2012
[49] Case No COMP/M.4942- NOKIA / NAVTEQ [2008] para 364
[50] Case No COMP/M.5389 *AEROPORTS DE PARIS / THE NUANCE GROUP* [2009] Para 38

In establishing whether the merger is likely to lead a significant impediment to effective competition, it is necessary to take into account any relevant efficiency. In TomTom/TeleAtlas case, the Commission identified merger specific efficiencies in the elimination of the double mark-up and to ability to produce better maps faster by sharing data, something the parties were unlikely to commit to without the certainty afforded by common ownership.[51]

2. CUSTOMER FORECLOSURE

According to guidelines customer foreclosure may occur when a provider merges with a significant customer in the downstream market. As a result of this downstream presence, the merged entity may foreclose access to an adequate customer base to its actual or possible rivals in the upstream market (the input market) and decrease their ability or incentive to compete. In turn, this may increase downstream rivals' costs by making it harder for them to get supplies of the input under same conditions as absent the merger. Consequently, merged entity may profitably establish higher prices on the downstream market.[52]

The six stages for analysing input foreclosure issues are equally applicable to the analysis of customer foreclosure issues.

a. Identify the leveraging conduct

A merged group may seek to pursue a customer foreclosure strategy for example by ceasing to purchase from upstream competitors, reducing its purchases from upstream competitors or carrying on purchasing from upstream competitors yet on less favourable terms than it would have done absent the merger.[53]

b. Analyse whether the merged group will have the ability to pursue the leveraging conduct;

In order for a customer foreclosure strategy to be practicable, the merged group must be an important customer and it must be capable of impairing the ability of upstream rivals to compete.

[51] Case M.4854 *TOMTOM / TELE ATLAS* [2008] para 238-250
[52] Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings 2008/C 265/07 para 58
[53] Ibid, para 60

After the merger if a large number of independent customers for the input remain, it is unlikely that a customer foreclosure strategy will have any impact on upstream rivals.[54] In Rozier/BHS case, the commission excluded customer foreclosure concerns on the grounds that the downstream customer would represent only a little part of the total demand for the input product.[55]

Similar to the assessment of input foreclosure, it is important to consider the various ways in which rival input suppliers sell the product or service, the customers to whom they sell, and the extent to which they can continue to sell sufficient volumes of the product or service without selling to the merged entity. It is also important to consider the extent to which downstream customers in the merchant market may be "freed up" as a consequence of the merged entity switching to use captive inputs.[56]

c. Analyse whether the merged group will have the incentive to pursue the leveraging conduct;

Assessing the merged group's incentive to pursue a customer foreclosure strategy involves analysing the various ways in which the merged group's profits will be affected and assessing whether the overall impact will be positive. Those ways could be analysing the increase in costs arising from transfer to self-supply and the impact on the merged group's profits on the upstream market.[57]

The other steps are identifying the foreclosure effect, assessing the causal link between the merger and the foreclosure effect and lastly considering any efficiency. Since those elements are shortly analysed above and due to lack of enough space, these elements will not further be analysed deeply.

3. ACCESS TO CONFIDENTIAL INFORMATION

[54] Ibid., para 61

[55] Case COMP/M.4788 — Rozier/BHS [2007] para 18

[56] Mat Hughes and David Wirth, 'The Assessment of Non-Horizontal Mergers Under EC and UK Merger Control' (2010) ICLG to: Merger Control <http://www.iclg.co.uk/khadmin/Publications/pdf/3237.pdf> accessed 12 April 2012

[57] Alistair Lindsay and Alison Berridge, EC Merger Control: Substantive issues (3rd edn, Sweet & Maxwell 2009) p.430

According to guidelines on the assessment of non-horizontal mergers, by vertically integrating the merged entity may gain access to commercially sensitive information regarding the upstream or downstream activities of rivals.[58]

The commission, in TomTom/Tele Atlas case, rejected concerns arose by third party PND producer that they had to share confidential information with upstream map suppliers on the basis that customers ultimately had full control over the type and amount of information revealed to Tele Atlas and the other map suppliers. In assessing whether a vertical merger is likely to give rise to concerns regarding the switch of confidential information, in TomTom/Tele Atlas decision the commission stated some factors to be taken into consideration. Firstly, it examined what information was actually exchanged between Tele Atlas in the upstream market and its customers and the extent of the flow of information in the pre-merger situation. Secondly, it considered whether such information flows between the upstream and downstream markets could be limited without harming consumers in the downstream market. And thirdly, it considered whether the merged entity would have the incentive to act on the confidential information to the benefit of the merged entity's downstream business. In assessing the incentives of the merged entity, the Commission observed that it is important to assess whether the merged entity would be willing to let customers move to NAVTEQ, an alternative supplier, due to confidentiality reasons.[59]

In Nokia/NAVTEQ case, third parties also stated their concern that access to information regarding the future actions of its downstream customers, would let the merged entity to displace any of their actions to win more customers through better prices, innovative features, new business concepts, increased coverage of map databases. However, the Commission found that the amount of information of competitive value exchanged between NAVTEQ and its customers related to their future behaviour is limited and could be further minimized. In this regard, customers did not need to exchange information in terms of the features in their new devices with NAVTEQ, as the involvement of independent software developers enabled

[58] Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings 2008/C 265/07 para 78
[59] Mat Hughes and David Wirth, 'The Assessment of Non-Horizontal Mergers Under EC and UK Merger Control' (2010) ICLG to: Merger Control <http://www.iclg.co.uk/khadmin/Publications/pdf/3237.pdf> accessed 12 April 2012

handset manufacturers to avoid direct contact with NAVTEQ and avoid the exchange of sensitive information.[60]

4. FORECLOSURE OF NEW ENTRY and OTHER CONCERNS ARISING FROM VERTICAL INTEGRATION

Vertical integration may create a barrier to entry if potential entrants need to enter two markets rather than one. Beside foreclosure of new entry there are other concerns arising from vertical integration such as coordinated effects and express collusion, price discrimination or reduced incentive to engage in research and development.

IV. CONCLUSION

The publication of the Non-horizontal merger guidelines had a little effect on the Commission's approach since the commission was already applying that approach in practice. In other words, the evolving approach of the Commission on non-horizontal mergers reached the same level as the guideline with GE/Honeywell decision before the guideline is adopted. Before adopting the non-horizontal merger guidelines, the decision of the commission and the community courts were lack of clarity. While in Skanska case, the ability of merged entity's foreclose the rivals costs were the main focus of the commission, in Tetra Sidel case, the ability and the incentive of the merged entity to foreclose rivals were the main focus of the commission and there are other different approaches of the commission which were examined above. The most significant case is the GE/Honeywell case, and in this case the commission examined both ability and incentive of the merged entity to foreclose rivals' costs and the impact that such foreclosure would have on consumer. This decision creates for the commission organizing principles for the assessment of non horizontal mergers. However, it has to be emphasised that publication of the Non-horizontal merger guidelines had a little effect on the Commission's assessment because the commission already started applying that approach in practice. In the guidelines there are three main possible concerns can arise from vertical mergers which are input foreclosure, customer foreclosure and access to confidential information. Input foreclosure takes place when the merger is likely to raise the costs of downstream rivals by restricting their access to an important input. Customer foreclosure takes place when the merger is likely to foreclose upstream rivals by restricting their access

[60] Mat Hughes and David Wirth, 'The Assessment of Non-Horizontal Mergers Under EC and UK Merger Control' (2010) ICLG to: Merger Control <http://www.iclg.co.uk/khadmin/Publications/pdf/3237.pdf> accessed 12 April 2012

to a sufficient customer base. And the last concern arises when the merged entity able to gain access to confidential information on its rivals. On its decisions after the adoption of the guidelines, the commission assess foreclosure in vertical mergers as anti competitive if it fulfils all the elements of the three-part test which are ability to foreclose, incentive to foreclose and likely impact on effective competition. As it is clearly seen, unlikely past practices, the Guideline put the parties' economic incentive to foreclose as a central and necessary element in the commission's merger assessment. This three part test first applied to the TomTom/TeleAtlas and Nokia/Navteq cases and the commission cleared both transactions after deep investigations, since in both cases the parties would found to have no incentive to foreclose their downstream competitors. It has to be additionally noted that vertical mergers may give rise to some efficiencies such as lowering transaction costs, saving costs through technological economies of integration, providing an assurance of supply of key inputs, avoiding successive mark-ups or eliminating market power. These efficiencies are important part of commission's assessment since they may lead commission not to block the merger.

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