

## An Assessment of the Immediate and Possible Longterm Effects of the New Substantive Test

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### **ABSTRACT**

*The new Merger Regulation, i.e. Council Regulation No 139/2004, introduced some important changes including the new substantive test. In this paper I will focus on the effect of the SIEC (significant impediment to effective competition) test by considering the recent decisions of the European Commission. This article analyses the differences between the SLC (substantial lessening of competition) test and the SIEC test, and the impact of the new test on merger policy, standard of proof, intervention threshold and market definition. The paper also discusses whether the new test would be stricter than the SLC test, whether it would avoid spill-over effects and whether it would lead to uncertainty in merger policy.*

### **ÖZET**

*Yeni Birleşme Tüzüğü (Konsey Tüzüğü, No 139/2004), yeni testi de kapsayacak şekilde önemli bazı değişiklikleri içermektedir. Bu çalışmada AB Komisyonu'nun yeni kararları çerçevesinde RET (etkin rekabetin önemli ölçüde engellenmesi- Rekabetin Engellenmesi Testi)'in etkileri ele alınacaktır. Makale, RAT (etkin rekabetin önemli ölçüde azaltılması – Rekabetin Azaltılması Testi) ile RET'in farklarını; yeni testin birleşme/devralma politikası, ispat standardı, müdahale eşiği ve pazar tanımına etkilerini incelemektedir. Çalışmada ayrıca yeni testin RAT'dan daha katı olup olmayacağı, kavram karışıklığına engel olup olmayacağı, birleşme/devralma politikasında belirsizliğe yol açıp açmayacağı tartışılmıştır.*

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**KEYWORDS:** *EU Merger Regulation 139/2004, significant impediment to effective competition (SIEC) test, unilateral effects.*

**ANAHTAR KELİMELER:** *AB Birleşme Tüzüğü 139/2004, RET (etkin rekabetin önemli ölçüde engellenmesi- Rekabetin Engellenmesi Testi), tek yanlı etkiler.*

The year 2004 will be remembered not only for the enlargement of the EU with ten new member states, but also as a year of transition for EU merger control. The European Commission launched the debate on the Merger Regulation 4064/89, which was amended by regulation 1310/97, in its Green Paper on the Review of Council Regulation (EEC) No 4064/89<sup>1</sup> at the end of 2001. After the Commission invited contributions from member states, the business community, legal community and other interested parties<sup>2</sup>, the Council of Ministers adopted the new regulation on November 27, 2003 following lengthy discussions. The enactment of Regulation 139/2004<sup>3</sup>, which came into force on May 1, 2004, introduced significant procedural, jurisdictional and substantive changes including the new test.

The new test, the “significant impediment to effective competition” (hereinafter “the SIEC test”), created a legal basis for the Commission to prohibit mergers giving rise to non-coordinated effects, which was recognized by the 1992 US Horizontal Merger Guidelines<sup>4</sup> as a part of the “substantial lessening of competition” test (hereinafter “the SLC test”). Therefore, some argue that the new reform brought the EU merger policy closer to the US merger regime and replaced the dominance test (hereinafter: the MD test) with a US-style test.

The new ECMR introduced the new substantive test in Article 2(3) on the appraisal of concentrations as follows:

A concentration which would significantly impede effective competition, in the common market or in a substantial part of it, in particular as a result

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<sup>1</sup> Green Paper on the review of Council Regulation (EEC) No 4064/89, COM (2001), 745/6 Final (hereinafter Green Paper), Brussels 11.12.2001

<sup>2</sup> For the submissions on the Green Paper, see <http://www.europa.eu.int/comm/competition/mergers/review/comments.html>.

<sup>3</sup> Council Regulation (EC) No 139/2004 of 20 January 2004 on the Control of Concentrations between Undertakings, [2004] O.J. L24/1 (hereinafter: the ECMR).

<sup>4</sup> US Horizontal Merger Guidelines, US Department of Justice and the Federal Trade Commission, 1992 (Revised 1997), § 2.1.

of the creation or strengthening of a dominant position, shall be declared incompatible with the common market.

The former wording of the same article referred to the creation or strengthening of dominance as the key criterion and a prerequisite for the significant impediment to effective competition. In theory the new test, the SIEC test, requires only the second prong of the MD test and accepts the created/strengthened dominance as “the primary form of competitive harm.” Therefore, this approach is a “hybrid” between the SLC and the dominance tests. I focus below on some questions stemming from the adoption of the SIEC test.

**Are the SLC test and the SIEC test synonymous? If not, what is the difference?**

The critical question is whether these two tests are identical or not. Vickers states that one interpretation is that they are synonymous, whereas the other approach claims that “substantial lessening” relates to how much competition is *lost*, while “impediment to effective competition” has to do with how much competition *remains* after the merger<sup>5</sup>. The second approach, to which Vickers refers, is echoed by Lang, a former high level official of the Commission, as follows:

The [former] regulation is based on the result (dominance or increased dominance), rather than the significance of the change resulting from the merger. Substantially reduced competition is not necessarily dominance: dominance is a result of how much competition is *left*, not how big the *change* has been.<sup>6</sup> (Emphasis added).

However, the difference is a “hybrid” of these two approaches: the new test considers how much competition is left and/or lost depending on the market structure.

Although both tests rely on market structure<sup>7</sup> and presume the anticompetitive effects of horizontal mergers by means of unilateral and coordinated effects, there exist some differences between them, which occur due to the Commission’s reluctance to move away from the dominance concept.

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<sup>5</sup> John VICKERS, “Merger Policy in Europe: Retrospect and Prospect”, ECLR, 2004, issue: 7, pp. 455-463 at 460

<sup>6</sup> John Temple LANG, “Oligopolies and Joint Dominance in Community Antitrust Law”, Fordham Corporate Law Institute (ed. Hawk, B.), 2001, vol.28, pp. 269-360 at 310

<sup>7</sup> Stefan VOIGT and André SCHMIDT, “Switching to Substantial Impediments of Competition (SIC) can have Substantial Costs-SIC!”, ECLR, 2004, issue: 9, pp.580-586 at 585.

First, these distinctions stem from the Guidelines<sup>8</sup> and the new ECMR. The ECMR declares that the SIEC test will be interpreted “beyond the concept of dominance”, *only* in respect of the anticompetitive effects of a merger resulting from the unilateral actions of the firms if they did not have a dominant position. Hence, it may be argued that the SIEC test is an MD test including unilateral effects below the dominance level. This fact is also underlined in Recital 26 which declared that the SIEC generally results from the creation or strengthening of a dominant position. Therefore the Commission should preserve the guidance that can be drawn from past decisional practice and past case law of the Community Courts, “while at the same time” maintaining consistency with the standard of competitive harm, including unilateral effects.

Second, decisions after the adoption of the SIEC test clarify its difference from the SLC test. As Baxter and Dethmers argue, the Commission has the legal basis to apply both unilateral effects and the dominance theories of harm, which can be drawn from recent cases. In most of the cases since the adoption of the SIEC, the Commission considered only single firm dominance, whereas in some cases it applied both theories *simultaneously*.<sup>9</sup>

In order to analyse the Commission’s approach to the SIEC test, it is necessary to focus on the recent cases. In *Seiko/Sanyo*<sup>10</sup> the Commission concluded that the market shares of the industry “suggest[ed] that single dominance, unilateral effects or collective dominance [were] not likely to result from the transaction.” Although the Guidelines – similar to the US Guidelines – declare that the anticompetitive effects of horizontal mergers may occur in two ways, i.e. unilateral and coordinated effects, it may be argued that the Commission considers three different ways: single dominance in addition to the other two harms of competition. The *Seiko/Sanyo* decision emphasized this distinction. Moreover, in *Repsol/Shell* this approach is highlighted:

The combined entity’s market share in itself excludes the possibility of the merger leading to the creation or strengthening of a dominant position. Also with regard to unilateral effects, Repsol and Shell are clearly not each other’s closest substitutes, as their geographical coverage is complementary.<sup>11</sup>

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<sup>8</sup> Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings (2004/C 31/03), [2004] OJ C31/5 (hereinafter: the Guidelines).

<sup>9</sup> Simon BAXTER and Frances DETHMERS, “Unilateral Effects Under the European Merger Regulation: How Big is the Gap?”, ECLR, 2005, issue: 7, pp 380-389 at 381-382.

<sup>10</sup> Case COMP/M.3459 *Seiko/Sanyo Epson Imaging Devices JV*, [2004], para. 13

<sup>11</sup> Case COMP/M.3516 *Repsol YPF/Shell Portugal*, [2004], para. 16

Hence, due to these three main anticompetitive effects, in some cases the Commission considers *only* the single dominance and concludes that “the proposed transaction will not lead to the creation or strengthening of a dominant position, as a result of which effective competition would be significantly impeded in the common market or a substantial part thereof.”<sup>12</sup> Whereas in the *Johnson & Johnson/Guidant* decision, unilateral effects and single dominance are applied *simultaneously* in steerable guidelines:

... it seems unlikely that remaining competitors and potential entrants can constitute a sufficient and timely competitive constraint such as to prevent a *unilateral increase* in prices by the merged entity. Further, it cannot be excluded that the remaining firms in the market may even be expected to benefit from the reduction in competition which will result from the merger; the increase in concentration may provide them the opportunity to attain higher prices than would otherwise have been the case. The merger is therefore likely to result in a significant impediment to effective competition [...] for steerable guidewires as a result of the strengthening of Guidant’s *dominant position*.<sup>13</sup> (Emphasis added.)

These interpretations lead to the consideration of whether the SIEC test has only one prong. Although the new wording of Article 2(3) presumes significant impediment to effective competition as the *only* prong and the dominance as the primary form of anticompetitive effect, the application of the Commission leads one to think that these two are independent prongs of the new test. In the MD test, the dominance *and* impediment to competition are two tiers; however, the application of the SIEC test includes the dominance *or* significant impediment as two independent prongs. Therefore, the Commission first considers whether the creation or strengthening of a dominant position will occur and if not, it *may* focus on the analysis of unilateral effects<sup>14</sup>. However, it is not clear why in some cases the Commission considers unilateral effects below the level of dominance and why it does not refer to this type of harm in most of its other

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<sup>12</sup> Case COMP/M.3836 *Goldman Sachs/Pirelli Cavi E Sistemi Energia/Pirelli Cavi E Sistemi Telecom*, [2005], para.29, see also Case COMP/M.3813 *Fortune Brands/Allied Domecq*, [2005], para.16

<sup>13</sup> Case COMP/M.3687 *Johnson & Johnson/Guidant*, [2005], para. 196, see also Case COMP/M.3751 *Novartis/Hexal*, [2005], para.5, Case COMP/M.3465 *Syngenta CP/Advanta*, [2004], para.52

<sup>14</sup> However, Levy argues the opposite without giving any reference to the recent decisions: “The Commission generally focuses first on unilateral exercises of market power and then on whether a transaction creates or strengthens a position of collective or oligopolistic dominance.” (Nicholas LEVY, *EU Merger Control: A Brief History*, Cleary, Gottlieb, Steen & Hamilton, Brussels 3 February 2004, p. 4, [http://www.cgsh.com/files/tbl\\_s47Details%5CFileUpload265%5C268%5CCGSH\\_CGSH\\_Paper\\_IBC\\_Conference\\_EU\\_Merger\\_Control\\_-\\_A\\_Brief\\_History.pdf](http://www.cgsh.com/files/tbl_s47Details%5CFileUpload265%5C268%5CCGSH_CGSH_Paper_IBC_Conference_EU_Merger_Control_-_A_Brief_History.pdf)).

decisions and focuses only on the dominance concept. This type of application of the SIEC test, therefore, may result in legal uncertainty.

On the other hand, this application of the new test creates another question: is the SIEC test stricter than the SLC test, since it has one additional “weapon” to block a merger? The new test may be stricter in some situations where the MD test is stricter than the SLC test. In addition to some theoretical arguments such as “chains of small mergers”<sup>15</sup>, there may be some different results due to distinctions between the two concepts. The SIEC test would block a merger depending on the dominance concept in a market where there is currently little competition due to the high barriers to entry and capacity constraints of competitors. In such a market, a merger could probably not create a change in competition and in SLC. However, the new test could prohibit this merger if it creates or strengthens a dominant position<sup>16</sup>. A similar example can be found in the merger of Boeing and McDonnell Douglas (MDD) where both the FTC and the Commission cleared the merger but focused on different factors. Boeing’s market share was 60 percent and increased by 10 percent as a result of the merger, whereas the market share of the only competitor, Airbus, was 30 percent. No further competitive attacks were expected from MDD due to the fact that the firm did not stand a chance in the competition for new orders. Therefore the FTC cleared the merger at an early stage; however, the Commission considered it critical because post-merger structure would strengthen Boeing’s dominant position. The critical point was that the FTC did not focus on Boeing’s dominant position and how the merger would affect the relationship with Airbus in terms of competition<sup>17</sup>. In general, although the SIEC test may be stricter in some situations than the SLC test, it is difficult to predict the Commission’s approach in these situations due to the limited case law.

On the other hand, with the introduction of the SIEC test, some argued that the focus of the SIEC test was on the competitive effects of the merger on competitors, customers and consumers, but not on dominance and market

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<sup>15</sup> Assume a market where the leading firm has 30 per cent of the market and the other 35 firms each have 2 per cent with a total of 70 per cent. If the leader decides to merge with other firms in the market, it would be blocked under the MD test when its market share exceeds the traditional 40 per cent threshold. However, the SLC test may clear every merger, as each one does not entail a “substantial” lessening of competition.

<sup>16</sup> OECD Directorate for Financial, Fiscal and Enterprise Affairs Competition Committee, Substantive Criteria Used for the Assessment of Mergers, DAF/COMP(2003)5, 11 February 2003, p 38, <http://www.oecd.org/dataoecd/54/3/2500227.pdf>

<sup>17</sup> See the discussion paper prepared by the Bundeskartellamt: Prohibition Criteria in Merger Control – Dominant Position versus Substantial Lessening of Competition?, 8 and 9 October 2001, p 22, <http://www.bundeskartellamt.de/wEnglisch/download/pdf/ProPap01-Mantel-e.pdf>

structure. Moreover, the new test was seen as changing EC merger control policy to a “more rigorous economic assessment”, “higher analytical and evidentiary standards” and “a new economic professionalism”.<sup>18</sup> However, as explained above, these arguments are somehow “optimistic”. As Baxter and Dethmers stated, since the introduction of the SIEC test, the Commission has not focused on unilateral effects in more than 70% of its decisions; but considers *only* an assessment of single dominance in these cases<sup>19</sup>. This approach may give some signals on the possible differences between the SLC and the SIEC tests.

### **Would the intervention threshold be lower with the SIEC test?**

Some commentators, particularly within industry, argued that a US-style of substantive test would lead to interventionist merger control. Some respondents to the Green Paper claimed that “lowering the threshold” by means of that test would allow the Commission to have unacceptably broad discretion in analysing merger cases and might put a “dangerous weapon” into the hands of the Commission<sup>20</sup>.

On the other hand, others claimed that the new test did not lower the intervention threshold<sup>21</sup>, but might be interpreted, at most, as “widening” the scope of the substantive test, due to the fact that it catches non-coordinated effects after the merger, whereas the MD test would not. This argument was echoed by two European Commission officials,<sup>22</sup> referring to some cases of the Court in which it declared that the Commission under the former test would assess “whether the concentration which has been referred to it leads to a situation in which effective competition in the relevant market is significantly impeded”, such as in *France v Commission*<sup>23</sup>.

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<sup>18</sup> Jessica SCHMIDT, “The New ECMR: “Significant Impediment” or “Significant Improvement?””, CMLRev, 2004, vol:41, pp 1555-1582 at 1567, 1568.

<sup>19</sup> BAXTER and DETHMERS, 2005, at 382.

<sup>20</sup> Summary of Replies to the Green Paper, point 102, [http://www.europa.eu.int/comm/competition/mergers/review/comments/summary\\_publication.pdf](http://www.europa.eu.int/comm/competition/mergers/review/comments/summary_publication.pdf)

<sup>21</sup> The Director General of DG Competition, Philip Lowe, stated that, “The test should not be interpreted as a lowering of the intervention threshold. Indeed, the “SIEC” already constitutes the base-line threshold ... The standard of incompatibility of mergers will therefore remain the same as before”, Implications of the Recent Reforms in the Antitrust Enforcement in Europe for National Competition Authorities, Italian Competition /Consumers Day, Rome, 9 December 2003, p 9, [http://europa.eu.int/comm/competition/speeches/text/sp2003\\_067\\_en.pdf](http://europa.eu.int/comm/competition/speeches/text/sp2003_067_en.pdf)

<sup>22</sup> Kyriakos FOUNTOUKAKOS and Stephen RYAN, “A New Substantive Test for EU Merger Control”, ECLR, 2005, issue: 5, pp 277-296 at 291-293.

<sup>23</sup> *France v Commission*, C-68/94, [1998] ECR I-1375, para.221.

However, the argument that these judgments signify that the SIEC was already the baseline threshold for merger control is not entirely convincing. First, the CFI interpreted the dominance prong of the MD test as a prerequisite for the "SIEC". Thus, in *France v Commission*, since the total market share of the firms was 60 percent<sup>24</sup>, the ECJ underlined the importance of the SIEC. Therefore, the baseline of the threshold was the dominance prong and the SIEC prong was considered as an addition to it.

Second, as Baxter and Dethmers argue, there are three reasons to believe that the threshold for intervention is lower under the SIEC test. These are; first, a reduction of the market share threshold from 40-50 per cent to 25 per cent with the new ECMR<sup>25</sup>; second, the introduction of a set of HHI thresholds in Guidelines, which correspond to the lower than the market share threshold of 25 per cent; and third, the possibility that the Commission's approach to product market definition may result in narrowly-defined markets due to the unilateral effects theory which focuses on closeness of substitution rather than the analysis of the relevant product market<sup>26</sup>.

Third, recent decisions of the Commission underline the fact that the intervention threshold is below 40 per cent due to the unilateral effects. For instance, in *Novartis/Hexal*, the parties' combined market share in the OTC M2A (Topical Anti-Rheumatics) product market amounted to 35-40 per cent in Germany. The Commission implicitly accepted that the merger did not create a dominant position by declaring this market share to be "relatively limited", but it expressed concern about possible unilateral effects after the merger.<sup>27</sup> Also, in *Syngenta/Advanta*, the Commission stated that the merger raised serious doubts since it might significantly impede effective competition in seven member states in the market for sugar beet seed. However, in *France and Belgium*, where the combined market shares would be 40-50 per cent and 50-60 per cent, respectively, it concluded by expressing concern about the creation of non-coordinated effects in the market rather than the creation of dominance, although in the post-merger market structure the merged firms would be the

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<sup>24</sup> *Ibid*, para. 226.

<sup>25</sup> Recital 32, ECMR. Although the 25 per cent market share threshold was also introduced under the old ECMR at Recital 15, due to the "well-established case law", a 40 per cent threshold has been applied. With the adoption of non-coordinated effects, the dominance limb is not compulsory, hence it is expected that the threshold will reduce to 25 per cent.

<sup>26</sup> BAXTER and DETHMERS, 2005, at 384, 385.

<sup>27</sup> Case COMP/M.3751 *Novartis/Hexal*, [2005], para.5, see also case COMP/M.3943 *Saint-Gobain/BPB*, [2005], para.105, where the combined market share of the merged entity would be around 30-35% in Denmark and in France, the Commission focused on a unilateral price increase by analysing production expansion of rivals and substitution between Saint-Gobain and BPB suspended ceiling products.



leader in both of these countries,<sup>28</sup> Therefore it may be argued that the Commission considers unilateral effects within the meaning of the new test where it concludes or has some doubts that the merger would not result in the creation or strengthening of dominance. This application may lead to a conclusion that the new test would result in lowering the threshold by extending beyond the concept of dominance, rather than “widening” the scope of the “old” substantive test.

### **Would the SIEC test lead to a radical change in merger policy?**

The effect of the new substantive test upon EU merger policy can be analysed from four perspectives. First, the historical background of the new test underlines the fact that the Commission is reluctant to introduce any radical change in merger control. The desire of the Commission to retain the MD test, rather than to change to an SLC test in order to maintain the “sizeable body of case law,” can be found in the Draft Merger Regulation, particularly in the proposed Article 2(2), which aimed to enlarge the concept of dominance to include unilateral effects by referring to a dominant position “without coordination” within the members of an oligopoly.<sup>29</sup> Therefore, the Commission proposed to insert a new substantive test, which aimed to clarify the concept of dominance under the ECMR in order to improve legal certainty,<sup>30</sup> In addition to this, the Commission argues that “the dominance test and SLC have produced broadly convergent outcomes and the dominance test is proving to be an instrument capable of being adapted to a wide variety of situations where market power exists.”<sup>31</sup> Hence, according to this view, a radical change in merger policy is not necessary.

Second, the new ECMR and the new Guidelines include some provisions permitting the adoption of the SIEC test without leading to a radical change. The Guidelines declare that most cases of incompatibility will continue to be based on the dominance concept, hence the Commission should preserve the past decisional practice and past case law of the courts. Moreover, it analyses the factors that would have to be taken into account in order to assess the non-coordinated effects by referring to past judgments and decisions. Therefore, even non-coordinated effects would be considered under the guidance of the application of both the Commission and the Community courts<sup>32</sup>. In addition to

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<sup>28</sup> Case COMP/M.3465 *Syngenta CP/Advanta*, [2004], paras 32-52.

<sup>29</sup> Proposal for a Council Regulation on the control of concentrations between undertakings, COM (2002) 711.

<sup>30</sup> *Ibid*, para. 55.

<sup>31</sup> *Ibid*, para. 54.

<sup>32</sup> ECMR, Recital 26.

this, the ECMR also expects that the SIEC would generally result from the creation or strengthening of a dominant position and in Article 2(3) it underlines the special position of dominance in the assessment of the new test.

Third, recent decisions on the application of the SIEC test clarify that there will be no essential change in merger control. In most of its decisions since the introduction of the new substantive test, the Commission considers only the assessment of single dominance, as explained above.

And last, as was found in a survey, there have been few cases in the application of the DOJ and the FTC in which the merged entities' market shares were below the traditional threshold and in which there was an absence of or little likelihood of coordination between the members of the oligopoly that the collective dominance could not catch.<sup>33</sup> Since the crucial change with the adoption of the new test is unilateral effects, there will probably be few cases that would be blocked as a result of the non-coordinated effects.

On the other hand, one may hope to see a fundamental change involving sophisticated econometric analysis to assess unilateral effects of harm, as the US agencies apply. As stated in the Green Paper, the Commission is aware of the importance of the sophisticated microeconomic tools, instruments and models developed by econometric and industrial organization research<sup>34</sup>. Moreover, some economic analyses are confirmed in the Guidelines which examine non-coordinated anti-competitive effects<sup>35</sup>. The appointment of the Chief Economist is further evidence of the Commission's desire to focus on economics.

However, these improvements may result in essential change in the long-term. In recent decisions, hardly any sign can be found of economic analyses. For instance, in the Novartis/Hexal case, the Commission stated its concerns about unilateral effects in the OTC M2A market in Germany by focusing on the degree of substitutability of the merging firms' products as follows:

Novartis is the undisputed market leader with its brand "Voltaren" (market share [30-35]%). Hexal's generic version "Diclac" (market share [0-5]%) is generally considered as a strong generic brand [...] Third parties have argued that "Diclac" is the closest substitute to "Voltaren"... [Other existing products on the market] are not close substitutes to "Voltaren" as

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<sup>33</sup> Sven B. VÖLCKER, "Mind the Gap: Unilateral Effects Analysis Arrives in EC Merger Control", *ECLR*, 2004, issue: 7, pp. 395-409 at 409.

<sup>34</sup> Green Paper, p. 39.

<sup>35</sup> Guidelines, para. 29.

they are not based on the same active ingredient as “Diclac” and “Voltaren”. The concentration would therefore combine two products which a substantial number of consumers would regard as their first and second choice. In such a situation, the parties have an incentive to increase prices post-merger. New entrants on the market were considered as not very likely, due to the high level of advertising costs to promote a new brand.<sup>36</sup>

The Commission focused on two factors: closeness and barriers to entry, in order to assess the unilateral effects. However, in the decision there is no evidence of economic analyses, as set out in the Guidelines, to evaluate the degree of substitutability, such as a customer preference survey, analysis of purchasing patterns, estimation of the cross-price elasticities or diversion ratios. Rather the Commission found the closeness of the merged firms’ products without a deeper analysis by only considering the third parties’ arguments and the structure of the rivals’ products. Hence, an essential change in merger policy to assess non-coordinated effects by means of the new test may only occur in the long-term.

On the other hand, the Commission’s approach to non-coordinated effects emphasizes that the market definition is probably becoming less important in the absence of dominance. For instance, in the Novartis/Hexal case the crucial question is not whether the product market should be defined narrowly or widely, but whether the products of the merging firms, Diclac and Voltaren, are closer substitutes than others or, in other words, whether consumer-switching behaviour occurs<sup>37</sup>. As the Guidelines state, the higher the degree of substitutability between these products, the more likely the parties are to have an incentive to raise prices post-merger. Hence, “the fact that rivalry between merging parties has been an important source of competition on the market”<sup>38</sup> may tend to the market definition being considered to be less important if there is no dominant position. However, this tendency is not an important change in merger policy, since it can be seen only in the absence of dominance such as 3 to 2 or 4 to 3 mergers.

### **Would the SIEC test avoid “spill-over” effects?**

Some commentators have argued that broadening the dominance concept by including non-coordinated effects in merger cases was at the same time broadening the category of companies to which the special rules in Article 82

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<sup>36</sup> Case COMP/M.3751 *Novartis/Hexal*, [2005], para.5.

<sup>37</sup> See also Case COMP/M.4007 *Reckitt Benckiser/Boots Healthcare*, [2006]

<sup>38</sup> Guidelines, para.28.

apply, due to the “spill-over” effects.<sup>39</sup> The new test – consistent with this argument -- focused on significant impediment to effective competition rather than the dominance concept, when the wording of Article 2 of the ECMR is considered. The application of the Commission, as stated above, also analyses unilateral effects within the meaning of the new test if there are any doubts that the merger would not result in the creation or strengthening of dominance. For instance in the Repsol/Shell case,<sup>40</sup> the Commission analysed the unilateral effects after finding an absence of dominance of the merging parties in retail markets. Moreover, this fact is underlined in the ECMR, since the SIEC test would be applied only to non-coordinated harm where a dominant position in the market does not exist.<sup>41</sup> Therefore, the decisions and the ECMR clearly emphasized that the dominance concept would not be widened by the adoption of the new test.

However, these two dominance provisions, which are used in merger control and in Article 82, are based on an identical concept, although each serves a different purpose. Therefore, in decisions where a dominant position is found rather than unilateral effects, there may still be “spill-over” or, as it is sometimes called, “cross-contamination” effects under the SIEC test, since the courts appear to consider the dominance concept as identical in both contexts,<sup>42</sup> such as in the judgement of the ECJ in the *Compagnie Maritime Belge* case.<sup>43</sup>

### **Would the SIEC test lower the standard of proof?**

“[... T]he contested decision does not establish to the requisite legal *standard* that the modified merger would give rise to significant anti-competitive ... effects ... It must therefore be concluded that the Commission committed a manifest error of assessment in prohibiting the modified merger on the basis of the *evidence*” (emphasis added).<sup>44</sup> That is the conclusion of the CFI in *Tetra Laval* which underlined the importance of the standard of proof in merger cases. Moreover, the CFI established a higher standard of proof in *Airtours* and added that “it was for the Commission to prove that ... [the] approval ... would have resulted in the creation of a collective dominant

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<sup>39</sup> Summary of Replies to the Green Paper, point 96.

<sup>40</sup> Case COMP/M.3516 *Repsol YPF/Shell Portugal*, [2004], para. 16.

<sup>41</sup> ECMR, recital 25.

<sup>42</sup> Summary of Replies to the Green Paper, point 96.

<sup>43</sup> Case C-395/96 P and 396/96 P *Compagnie Maritime Belge NV and Dafra-Lines v Commission*, [2000], ECR I-1365, para.41.

<sup>44</sup> Case T 5/02 & 80/02 *Tetra Laval BV/Sidel v Commission*, [2002], ECR II-4381, para. 336.

position restrictive of competition.”<sup>45</sup> Similarly, the CFI, both in the *Airtours* case and in the *Tetra Laval* case, declared that if the Commission considered blocking a merger on the grounds of the creation or strengthening of a dominant position, it would be incumbent upon the Commission to produce *convincing* evidence.<sup>46</sup> The ECJ in its most recent judgement in the *Tetra Laval* case declared that the CFI did not err in law when it specified the quality of the *evidence* which the Commission was required to present.<sup>47</sup>

At this point, it is necessary to highlight the differences between the concepts of burden of proof and standard of proof, as the courts underlined these two closely related concepts in recent cases. The standard of proof is a threshold that must be met before a court can reach a conclusion on the evidence before it, whereas the burden of proof is the act of presenting evidence needed to meet a required standard of proof.<sup>48</sup> Hence, the burden of proof focuses on “who has to prove”, while the standard of proof focuses on “what has to be proved”.

Although the “convincing evidence” sought by the Court is not clear, the following considerations may be argued on the grounds of recent case law. First, due to the freedom to merge, it is incumbent upon the Commission rather than the merging parties to prove that there are anticompetitive effects arising from non-coordinated or coordinated effects, which result in the SIEC. Second, the nature of proof in merger decisions differs from that in other cases, depending on Article 81 or 82, due to the fact that post-merger analysis depends on the prediction of future events rather than past evidence, as the ECJ stated in the *Tetra Laval* case:

A prospective analysis of the kind necessary in merger control must be carried out with great care since it does not entail the examination of past events – for which often many items of evidence are available which make it possible to understand the causes – or of current events, but rather a prediction of events which are more or less likely to occur in future if a decision prohibiting the planned concentration or laying down the conditions for it is not adopted.<sup>49</sup>

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<sup>45</sup> Case T-342/99 *Airtours plc v Commission*, [2002], ECR II-2585, para 77.

<sup>46</sup> *Ibid*, para. 63, Case T 5/02 & 80/02 *Tetra Laval BV/Sidel v Commission*, [2002], ECR II-4381, para. 155.

<sup>47</sup> Case C-12/03 P *Commission v Tetra Laval Bv*, [2005], para. 45.

<sup>48</sup> David BAILEY, “Standard of Proof in EC Merger Proceedings: A Common Law Perspective”, *CMLRev*, 2003, vol. 40, pp. 845-888 at 848, 849.

<sup>49</sup> Case C-12/03 P *Commission v Tetra Laval Bv* [2005], para. 42, see also case T-342/99 *Airtours plc v Commission*, [2002], ECR II-2585, para. 210.

Hence, third, a high standard of proof or “a close examination of the circumstances”<sup>50</sup> is crucial, because of the nature of the merger decisions. This level of proof is declared to be “standard of proof” which has to include “precise examination, supported by convincing evidence.” So, how could the Commission meet this convincing evidence standard? Is it necessary to establish whether the SIEC is more likely than not, or very likely, or beyond reasonable doubt, or even full proof (i.e. 100 %)? For convincing evidence, the Commission has to consider five crucial features, which underline the level of proof that the Commission has to assess:

Not only must the Community Courts, inter alia, establish whether the evidence is relied on accurate, reliable and consistent but also whether that evidence contains all the information which must be taken into account in order to assess a complex situation and whether it is capable of substantiating the conclusions drawn from it. [Emphasis added.]<sup>51</sup>

On the other hand, the ECJ stated that, in order to assess the “impediment to effective competition”, it is “necessary to envisage various chains of cause and effect with a view to ascertaining which of them are the most likely” (emphasis added).<sup>52</sup> Thus, it may be argued that the court does not impose on the Commission full proof by claiming most likely, but it also does not accept a certainty of 51 percent as the evidence has to be accurate and capable of substantiating the conclusions, therefore it may be concluded that a high level of certainty is necessary to block a merger.

Whether the standard of proof would change with the introduction of the SIEC test depends on the existence of dominance. If a merger creates or strengthens a dominant position, then there would be no change in the structure of the evidence, but if it is below the level of dominance, the Commission has to prove that the merger would lead to a SIEC in that market even where coordination does not exist. Hence, in that situation, i.e. in a market where unilateral effects occur, the Commission would not rely on market share (as in the assessment of dominance) and would not use evidence of past coordination or coordination in similar markets<sup>53</sup> (as in the coordinated effects). Therefore, the Commission should rely on economic analyses, which, although set out in the Guidelines, cannot be found in its recent decisions.<sup>54</sup> However, as discussed

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<sup>50</sup> Case C-12/03 P *Commission v Tetra Laval Bv* [2005], para. 40.

<sup>51</sup> *Ibid*, para. 41,39.

<sup>52</sup> *Ibid*, para. 43.

<sup>53</sup> Guidelines, para.43.

<sup>54</sup> *Ibid*, para. 29.

before, a high level of econometric analysis as evidence in favour of blocking a merger may be used in the long-term. The European courts' insistence on a high standard of proof may accelerate this improvement. As a result, with the adoption of the SIEC test, a high standard of proof may be necessary in a market where dominance and coordination do not exist.

On the other hand, although the *Gencor* judgment demonstrated that the burden of proof is not only incumbent on the Commission,<sup>55</sup> as the CFI stated in that case, that the applicant "has not disproved the Commission's analysis" and "the applicant has not adduced the necessary proof"<sup>56</sup>, in recent merger cases, the CFI strictly underlined that the burden of proof is on the Commission<sup>57</sup>. Since the ECJ declared that the CFI did not err in law in its judgement on the requirements of Article 2(3) of the former ECMR to be satisfied,<sup>58</sup> there would probably be no change with this strict burden of proof after the adoption of the SIEC test. This approach is consistent with the fact that in Articles 81 and 82 infringement decisions, the burden of proof is on the Commission<sup>59</sup>.

## Conclusion

Although merger control originated in 1951, the Council of Ministers did not adopt its first Merger Regulation until 1989. This earlier regulation referred to the dominance, rather than the market power concept. This was not only because of the familiarity with this concept in EU Law, but also due to the absence of any provision to control mergers. However, this approach to concentrations led to the "gaps" in the former test, although the Commission and the courts interpreted the dominance in a flexible structure. The aim of the adoption of the new ECMR and the new substantive test was to avoid these difficulties that faced the Commission. On the other hand, the likely impact of the application of the SIEC test can be concluded as follows below.

First, the new substantive test is a hybrid of the SLC and the MD tests. When the wording of Article 2(3) is considered, the SIEC test can be interpreted as similar to the SLC test rather than the MD test. In theory, the new test is required only to assess for the SIEC and hence has only one prong; moreover it considers the creation and strengthening of dominance as the primary form of SIEC, which was accepted as the one of the two

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<sup>55</sup> BAILEY, 2003, at 862.

<sup>56</sup> Case T-102/96 *Gencor v Commission*, [1999], ECR II-753, paras 234, 283.

<sup>57</sup> See e.g. case T-342/99 *Airtours plc v Commission*, [2002], ECR II-2585, para. 77.

<sup>58</sup> Case C-12/03 P *Commission v Tetra Laval Bv*, [2005], para 45.

<sup>59</sup> Council Regulation (EC) No 1/2003, [2003] OJ L1/1, Article 2.

prongs in the MD test. Therefore, in the light of the wording of Article 2(3), it may be claimed that these two tests are similar. However, the new ECMR, the Guidelines and decisions of the Commission underline the fact that the new test has two independent prongs: SIEC and the dominance concept. Hence, these two tests are not synonymous above the level of dominance on the grounds of application. On the other hand, with the lack of dominance these two tests focus on the effect on competition and may be similar to each other.

Second, the SIEC test is an MD test including unilateral effects in the absence of dominant position and this aspect of the new test may result in a stricter application than the SLC test.

Third, the new test would result in lowering the threshold by including non-coordinated effects below the level of dominance. For this reason, being a leader in the post-merger market structure is not essential, but some other factors that create non-coordinated effects by means of a reduction in the competitive constraints which would lead to significant price increases in the relevant market are also crucial to the analysis of the effects of the merger.

Fourth, due to the introduction of unilateral effects, market definition may lose its importance and the rivalry between the merging parties may somehow become more essential in the absence of dominant position.

Fifth, it is not expected that a radical change in merger policy will be seen as a result of the introduction of the SIEC test, except a deeper economic analysis, which may occur in the long-term.

Sixth, the new test did not enlarge the dominant concept by including non-coordinated effects, however it can hardly be argued that the SIEC test would avoid spill-over effects, i.e. confusion with Article 82.

Seventh, a high standard of proof, i.e. "convincing evidence", is incumbent upon the Commission and will be maintained after the adoption of the SIEC test. However, in order to assess unilateral effects, a stronger standard of proof would be necessary, as the Commission would not rely on market share and coordination.

Lastly, the fact that, in most of the cases since the introduction of the new test, the Commission has only analysed single firm dominance without any reference to unilateral effects may lead to legal uncertainty.



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Therefore in general, contrary to Fountoukakos and Ryan's arguments, it is not "a satisfactory ending to this particular story."<sup>60</sup> Nevertheless, the conclusions set out above depend on the limited number of decisions based on the SIEC test. As the Commission's approach to this subject is still in the process of development, there may be a move away from the dominance concept to market power through the interpretations of the European courts in the future.<sup>61</sup> However, the considerations below should be focused on in this transitory stage:

- The Commission should interpret the new test as an effects-based test. Hence, it should focus on the "significant impediment to effective competition" limb rather than the dominance concept, and would thus avoid legal uncertainty due to the usage of two theories of harm, namely dominance and unilateral effects.

- In order to assess SIEC, "high-tech" econometric analyses are crucial and would be compulsory in cases where the merging parties are not dominant and where there is an absence of coordination between the members of the oligopoly. This necessity may be considered as a result of strict standard of proof, which is incumbent upon the Commission, as the courts have underlined.

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<sup>60</sup> FOUNTOUKAKOS and RYAN, 2005, at 296.

<sup>61</sup> Moreover, the Guidelines also accept that the Commission should prevent mergers significantly increasing the "market power" of the firms in para. 8. Market power is also referred to in para.27.