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Collective Dominance

- Merger Control on Oligopolistic Markets

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Collective dominance - Merger Control on Oligopolistic Markets

Collective dominance means that two merging companies together with one or several other companies may give rise to a collective dominant position on the market, which may distort an effective competition. The concern is that the conditions for collusion between firms will be enhanced after the merger. Markets concerned are generally oligopolistic, which are characterised by few suppliers having important market shares without any element of single dominance. An increasing number of mergers have created a new issue for the competition policy. The attitude to mergers of the EU is basically affirmative in order to reinforce the competitiveness on the European market against, for instance, American and Japanese giants. Only in cases where these mergers risk restraining a fair competition, the Commission's intention to intervene is justified. In both the U.S. and in Europe, oligopolistic markets and how to control them are of great concern, since they are likely to impede effective competition. For instance, oligopolies are regularly discussed in the OECD meetings and the organisation has also published a number of documents concerning these markets.

1. Introduction

1.1 European Competition Policy

The requirement for a common European competition policy has been recognised from the very beginning of the foundation of the European Communities. Both the Treaty of Rome, establishing the European Coal and Steel Community, as well as the Treaty on the European Economic Community signed in Rome in 1957 contain a chapter on competition rules. The Treaty on European Community (hereinafter "EC") states that the Community's primary task is, by establishing a common market and an economic and monetary union to "promote throughout the Community a harmonious and balanced development of economic activities, sustainable and non-inflationary growth respecting the environment, a high degree of convergence of economic performance, a high level of employment and of social protection, the raising of the standard of living and quality of life, and economic and social cohesion and solidarity amongst Member States."[1] Article 3 EC establishes the activities and tasks of the EU to the general objectives set out in Article 2. To achieve these objectives, the Community's activities shall include "a system ensuring that competition in the internal market is not distorted."[2] According to Article 3 (g) EC, competition policy is indeed one particular part of the general economic policy of the Community. It implies the existence of a market of workable competition, that is to say the degree of competition necessary to ensure the observance of the basic requirements and the attainment of the objectives of the EC Treaty, in particular the creation of a single market.[3] The competition policy is not an objective in itself, but shall be seen as an instrument to obtain the fundamental goals of the Community and eliminate obstacles to the free movement of the four liberties. It should be noted that European competition policy is tempered not only by a unified market objective but also by the social objectives of the EC, inter alia, to ensure a high degree of employment. The European Commission, or more precisely, the General Directorate for Competition (hereinafter the Commission) has been entrusted to carry out these activities.

1.2 Merger Control Policy

The development entailing an increasing number of mergers seems not to cease. Globalisation and the creation of businesses with worldwide leadership result in more and more consolidated markets. One of the instruments that will ensure a sufficient degree of undistorted competition is the European Merger Control Regulation[4] (hereinafter the Merger Regulation). Merger control is important since it can prevent the creation of uncompetitive market structures. Preventative actions are better than remedial actions, since it is often difficult to find remedies that fully will re-establish the pre-merger competitive environment. Behavioural remedies imposed after an anti-competitive merger may not be fully able to address the root cause of the problem, which is the post-merger market structure. However, with the same tool, an overly enthusiastic enforcement policy or one that is unclear or unpredictable could lead to efficient mergers being prevented or deterred.

Before the Merger Regulation, which was adopted in 1989, the Commission was

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[1] Article 2 of the Treaty on European Community
[2] Article 3(g) EC Treaty, inserted by Article G (3) Treaty on European Union
[3] Confirmed by the Court in C-75/84, Metro-Saba v. Commission [1986] ECR 3021.
[4] Council Regulation (EEC) No 4064/89 (OJ L 395,30.12.1989) as amended by the Council Regulation (EC) No 1310/97 (OJ L 180, 9.7.1997).

limited to the application of Articles 81 and 82 EC (former Articles 85 and 86 EC) in order to prevent mergers that were likely to give rise to competition concerns. As the European Court of Justice (hereinafter the ECJ or the Court) held in Continental Can[5], these two articles offered limited possibilities to deal with concentrations. Article 86 (new 82) only gave the possibility to prohibit an already established dominant position, but not the creation of such a position[6]. The applicability of Article 85 (new 81) embraced only situations where the two companies remained independent units[7]. These limitations led to the creation of a specific instrument in 1989; the Merger Regulation. According to Article 2 (3) of the Merger Regulation "[A] concentration which creates or reinforces a dominant position as a result of which effective competition would be significantly impeded in the common market or in a substantial part of it shall be declared incompatible with the common market." According to the Merger Regulation, concentrations having a certain size[8] shall be notified to the Commission, which will carry out an analysis in order to assess whether the transaction is compatible with the competition policy or not. A "dominant position" has been defined by the Court as "a position of economic strength enjoyed by an undertaking which enables to prevent effective competition being maintained on the relevant market by giving it power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers. In general a dominant position derives from a combination of several factors which, taken separately, are not necessarily determinative." [9]

Another notable consequence of the globalisation and the specialisation in merger activity is the increased occurrence of mergers in markets that can be described as oligopolistic. However, the Merger Regulation does not contain any additional provision in respect to this matter and the competition authorities in Europe have during a long time been lacking of an efficient tool to regulate such markets. The market structure in oligopolistic markets often results in anti-competitive effects to the impediment of the consumers. The control of concentrations is based on the concept of dominance and the wording in Article 2 (3) refers to "a concentration

5 Case 6/72 Continental Can (1973) ECR 215
6 See supra note 5, para 26
7 Case 142 and 156/84 British American Tobacco Ltd and R.J. Reynolds Industries Inc. v. Commission
8 A merger has a "Community dimension" if certain thresholds are obtained. These are calculated from the merging companies turnovers – Europeanwide, worldwide and national.
9 Case27/76 United Brands Co v. Commission [1978] ECR 207, similar wording in Case 85/76, Hoffman-La Roche v. Commission, [1979] ECR 461.

which creates or strengthens a dominant position". For more than two years after the coming into force of the Regulation it was not clear whether collective dominance was embraced by this article. Collective dominance refers to a situation where the parties of the concentration together with one or more third parties may give rise to a collectively hold dominant position. Therefore, it was of greatest importance for the Commission to adopt a measure to regulate these markets. The Commission developed the concept of collective dominance in order to control transactions increasing the concentration to the point that firms, in oligopolistic markets, may act as if they had conspired without the need to enter into an agreement or concerted practice. This practice, the concept of collective dominance, was recognised by the ECJ in joined cases France and others v. Commission[10] in 1998 and later confirmed by the Court of First Instance (hereinafter the CFI or the Court) in Gencor v. Commission[11]. However, the concept is still surrounded by uncertainty. This thesis aims to provide some clarifications on this point.

2. Method

The Commission has provided a considerable number of cases, where collective dominance has been examined. The European Court Justine (hereinafter "the ECJ" or "the Court") dealt with collective dominance for the first time in Italian Flat Glass in a case concerning an infringement of Article 81. However, during the past few years, there has been a fast development of the concept of collective dominance relating to merger cases and the examination under the Merger Regulation. The cases from the Court have been particularly observed in this thesis. Apart from case law, articles and texts by legal experts as well as industrial economists have provided useful information.

2.1 Purpose and limitations of the scope

The purpose of this thesis is to find out how the European Merger Control Regulation is applied to situations of collective dominant position and to study how far the concept of collective dominance can be stretched by examining relevant case law. The concept of collective dominance applies to three sets of legal provisions; the Articles 81 and 82 as well as the Merger Regulation. Comparisons will be made

[10] Joined cases C-68/94 and 30/95 France and others v. Commission of 31 March 1998.

between these provisions, even though the focus will be on merger appraisals in oligopolistic markets. Initially I will try to explain the basic theories of oligopolistic markets and the outcome of collective dominance, which is tacit collusion and parallel behaviour. This will be followed by a study of relevant case law. I also intend to invoke some legal concerns regarding the application of the concept and the significant degree of unpredictability surrounding collective dominance, which makes it difficult for the firms to calculate the outcome of their behaviour as well as predicting the legal consequences of a prospective acquisition of a competitor. Finally, the focus will be on the criteria of the assessment of collective dominance.

3. Background

3.1 The provisions of the Merger Regulation

When making its appraisal the Commission must take into account a non-exhaustive list of factors, which are embodied in Article 2 (1) of the Merger Regulation, for example, the need to maintain and develop effective competition within the common market in view of, among other things, the structure of all the markets concerned and the actual and potential competition from undertakings located either within or outside the Community. Other important considerations regard the market position of the undertakings concerned and their economic and financial power, the alternatives available to suppliers and users, their access to supplies or markets, any legal or other entry barriers, supply and demand development for the relevant goods or services, the interest of the intermediate and the ultimate consumers, and the development of technical and economic progress.

These provisions are general, but should be taken into account when the Commission assesses the two criteria listed in Article 2 (3) of the Merger Regulation.

3.1.1 Article 2 (3)

A concentration shall be declared incompatible with the common market if it "creates or strengthens a dominant position as a result of which effective competition would be significantly impeded on the common market or a substantial part of it", according to Article 2(3) of the European Merger Regulation 4064/89 on the control of

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[11] T-102/96 Gencor v. Commission of 25 March 1999.

concentrations between undertakings.

3.1.1.1 Create or strengthen a dominant position

Unlike the merger practice in the U.S. the EC merger control establishes two criteria that have to be fulfilled in order for the Commission to block the concentration. First, the Commission examines whether the concentration creates or strengthens a dominant position. The second criterion focuses on whether the concentration will "significantly impede competition". The U.S. practice focuses exclusively on the latter one. A relevant question is why the creation or the reinforcement of a dominant position has to be established in order to prohibit a merger that will be of harm to the objectives of the competition policy. Nevertheless, it is clear that the two criteria interact, since dominance is based on the ability to influence the behaviour of its competitors, which corresponds to the size and the market power of the firm. Only concentrations that attain a certain so-called community dimension shall be notified to the European Commission. The community dimension is based on the turnover thresholds set out in Article 1 of the Merger Regulation. In cases of an alleged creation or reinforcement of a collective dominant position, the Commission analyses the post-merger market conditions. When examining the future market power of the merging companies, also the competitive influence of other companies will be taken into account. The outcome of the assessment of the concentration may be affected by the fact that the parties to the concentration together with another party would be able to collectively dominate the post-merger market. There is no indication to what extent other firms in the market are to be included in the calculation of market shares in order to obtain a sufficient degree of market power. In the decision Nestlé/Perrier[12] in 1992, the Commission decided to include oligopolistic markets under the Merger Regulation.

The assessment of collective dominance requires a detailed study of the market structure. In an examination of this feature, the market share serves us a clear quantitative indication. However, there are no fixed rules for how these market shares have to increase in order to create or reinforce a dominant position. A merger that risks to create a single dominant position can give rise to an examination if the combined market shares of the merging companies exceed 25 per cent, according to

[12] Case No IV/M.190-Nestlé/Perrier of 22.07.1992

the preamble of the Merger Regulation.[13] The parties' combined market shares are always assessed by reference to the positions held by their competitors. If they have a weak position, this reinforces the concerns. If the merging parties have a clear lead over their competitors, the merger may reinforce that lead. On the other hand, the merger may not significantly impede effective competition if it merely counterbalances a similar market position held by the competitors or if there is a considerable buying power of consumers. A strong market position may also be based on other factors, such as financial resources, technological leads and advantages in investment and research. Instability of market shares over time is a sign of effective competition, while stability may indicate either market dominance or effective competition.

3.1.1.2 Significantly impede effective competition

A dominant position may be strengthened even if the market share of the acquired party is very small. The key issue under Article 2 (3) of the Merger Regulation is whether a relatively small increase in market share is likely to reduce competition significantly. This is not unlikely when a firm that holds a dominant position in an oligopolistic market acquires a competitor, also if the competitor has a small market share.

4. Oligopoly

4.1 Oligopolistic markets

Microeconomics does not provide a precise definition of an oligopoly. However, it is assumed that an industry with few firms and many buyers would amount to one. The question of how few market participants there have to be in an oligopoly is not so important, since the result of the market in terms of price and output of the undertaking's behaviour is what matters. When the companies in a particular market realise that their individual decisions regarding output or price will lead to reactions on the market, the situation may be distinguished from both perfect competition and monopolistic markets and hence be qualified as an oligopoly. What is fascinating with this market theory is those economists have not been able to predict how the firms involved set their prices. This is why there are several theories about oligopoly.

[13] Recital 15 of the preamble to the Merger Regulation

However, there are basically two main conclusions concerning oligopolies. On one hand, the mere structure of the oligopoly might lead to a profit-maximisation since the conditions for tacit collusion are rather favourable. On the other hand, the competition on an oligopolistic market may be as active as in a situation of perfect condition, since the structure of the market still allows for a sufficient number of competitors.[14] This theory involves the assumption that the firms involved in such markets are cautious about raising prices. Therefore, it is not right to say, without getting into an economic analysis of the market, that simply because there is price rigidity there must be an ongoing collusion among the firms involved. Moreover, the fact that there is little price movement does not conclusively mean that competition is hampered. Although the Court now seems to have adopted an economic approach in establishing the existence of collusion, there may be a need for a better definition of what amounts to collusion. The importance of this lies, inter alia, in preventing non-collusive parallel conduct from being regarded as evidence of concerted practice. Therefore, it is of considerable legal importance for the Commission to provide guidelines to the operators in this area and to define the concept of tacit collusion. When assessing alleged concerted practice links between firms play a considerable role as evidence. In oligopolistic markets, the companies can be in a position of joint dominance without having been in contact with each other. Their behaviour is a result of the market conditions and other economic factors. The notion goes thereby less far than concerted practice. The companies in an oligopolistic market do not have to collaborate in order to attain something that reminds of a collective dominant position. When assessing collective dominance under the Articles 81 and 82, collusion has to be legally established. What in economic terms indicate the same result as if the parties colluded must be distinguished from the legal definition. In contrast, when the Commission examines a merger notification it does not have to legally establish collusion, but whether economic facts will make collusion likely in the post-merger market.

4.1.1 Tacit collusion

What sustains collusion has economically no relevance. Instead, what matters is the mechanism that makes the firms acting like they had agreed to a contract on price or on volume. In the short run, each firm has an incentive to cheat on the agreement, for

[14] Briones, Economic Assessment of Oligopolies under the Community Merger Control Regulation,

example by undercutting the agreed price. What prevent them from doing so are the long run consequences, as no contract can be written and hence not enforceable against them. These consequences are the threat that prices will fall much further in the future through punishments and reduce their own and collective profits. Thus what matters is not the exact mechanism by which firms can agree on a price increase, but the existence of a credible mechanism to keep prices at that level. In other words, if we interpret joint dominance as collusion in the economic sense, what is important in merger control is preventing co-ordination in circumstances where it looks likely that it could be sustained. The purpose of merger control shall therefore be to prevent, as far as possible, market structures, where the companies will have an incentive to co-ordinate their actions. The main feature of an oligopoly is the existence of a sustainable mechanism by which the threat of lower prices in future will make it rational for the large, remaining firms to stick together to the higher price, despite the fact that they in short term have an incentive to undercut the prices.

4.2 Price-fixing in oligopolistic markets

The main reason why firms do not raise their prices is because they would lose sales if they did so. Many of those sales will be lost because customers who previously would have bought from that firm will instead buy from its competitors. Although increased price result in benefits from a larger margin, the firm loses the margin that it was previously earning on the sales that now have migrated to its competitors. A rational profit maximising firm will set its prices at a level at which any further price increase would cost more in lost sales than it would benefit from the firm through wider margins on the retained sales.

4.3 Mergers in oligopolistic markets

Mergers can be horizontal, vertical or diversifying. As horizontal mergers occur between directly competing firms these are likely to threaten the maintenance of effective competition. Horizontal mergers can raise fears of unilateral effects, co-ordinated effects and exclusionary behaviour. Also vertical mergers, which are mergers between firms acting on different levels within the same supply chain, may give rise to competition concerns such as foreclosure of the market and collusion.

[1993] 3 ECLR p. 118.

4.3.1 Unilateral effects

Unilateral effects arise when two closely competing products are brought under common ownership. The term unilateral effect refers to the fact that the post-merger firm has an incentive to raise the price even if the merger has no effect on the behaviour of the competing firms. A significant constraint is likely to be eliminated if both parties earlier to the merger enjoyed significant pre-merger market shares or if they were particularly close substitutes for one another. These effects do not rely on the tacit co-operation of other firms in the industry, although under most models of oligopolistic behaviour the other firms will adjust their output and take account of the modified behaviour of the merged firms. If a firm acquires its closest competitor this will result in a wider margin on retained sales of those products, since the gap to the next competitor will be larger. Since some lost are regained in higher sales, the merged firm has an incentive to raise its prices.[15]

4.3.2 Co-ordinated effects

The second form of competitive harm which might flow from a horizontal merger is the risk that a reduction in number of firms and greater market shares held by one firm will lead to collusive price increases amongst all the firms in the market. The collusion may be explicit, in the sense that a formal cartel becomes viable or more stable following the merger. However, it may be that the reduced number of firms will make collusive behaviour more likely to take place so the firms collectively can benefit from ceasing to compete vigorously. Fewer firms and increased concentration may improve the mechanisms for detecting and punishing those who would try to cheat on any tacitly collusive agreement and the creation of a stable collusive arrangement becomes more likely. Unlike unilateral effects, co-ordinated effects are the result of the co-ordination of the behaviour of different firms. As with unilateral effects, the likelihood of the creation of co-ordinated effects will depend on other circumstances than the modification the concentration in the market. In fact, the conditions for a successful co-ordinated post-merger price rise are similar to the conditions required for a successful cartel, no matter whether the collusion is explicit or tacit.

In homogeneous markets, in which the products are undifferentiated, the most

[15] See for example the argumentation of the Commission in Case IV/M.1956 Volvo/Scania of 22.03.2000.

important concern may not be that the merged firm will engage in unilateral price rises, but that the entire market will become tacitly or explicitly collusive after the merger. Post-merger effects that rely on the behaviour of the merged firm's rivals are called co-ordinated effects, which are the possibility for the remaining parties to monitor the market, that is oligopolistic dominance. Since collusion is most successful in stable, predictable and transparent markets, such confounding factors might include the lack of transparency in pricing, a high degree of customisation, widely differing cost bases between suppliers, differing degrees of vertical integration and rapidly expanding and volatile demand. In the case of alleged co-ordinated effects, market shares may provide a reasonable preliminary indication of the competitive position in the market. Further investigation shall focus on the degree of product homogeneity, the degree of symmetries between firms in terms of their sizes and cost structures, and the level of transparency in the pricing and output. Also entry barriers are relevant for the assessment of the notified merger.

4.4 Characteristic of the market susceptible to oligopolistic dominance

The Merger Regulation does not expressly cover concentrations that reduce the number of suppliers in a market to two or three. In the case where a few suppliers account for most of the sales in the market, economists speak of oligopoly. In an oligopolistic market, depending on which economy theory is favoured, the market conditions might lead to the same results as perfect competition, as measured in price and output, or might result in a situation where monopolistic prices and output prevail. The question is whether this uncertainty will result in the need to restrict the enforcement of competition policy to monopolies and cartels only. The Commission includes oligopolies in the enforcement of the Merger Regulation by stating that when, as a result of a merger, two remaining firms will have large market shares, the concentration may under certain circumstances lead to a dualistic or oligopolistic dominant position. In some cases this position may entail the same anti-competitive effects as a situation of a single dominance.

The notion of oligopoly lacks the precision that can be accorded both to monopoly and to perfect competition.[16] The theory of interdependence holds that the structural conditions peculiar to oligopolies result in non-competition between the operators and

[16] Whish, Richard, Competition Law (1993) at p. 385

thus they will obtain supra-competitive profits without falling under the scope of Article 81. One theory claims that in an oligopolistic market, the rivals are independent resulting in an inevitably minimal or even non-existent price competition. As mentioned, in oligopolies it is not always necessary for the parties to enter into collusive agreements in order to earn supra-competitive profits. The structure of the market is such that through interdependence and mutual self-awareness the prices will rise towards prices significant to monopolistic markets.[17] The theory of inter-dependence tries to fill the gap between conspiracy and single dominance. Critics of the theory of interdependence claim that it too simplistically presents a picture of market structures and that it fails to explain why, in some oligopolistic markets, competition is so intense and how oligopolists can earn supra-competitive profits without actually colluding. From an economic point of view it can be seriously doubted that the assumption that an oligopoly produces the same anti-competitive effects as a single dominant position can hold.[18] Some economic theories claim that an oligopoly under certain circumstances produces the same positive effects with regard to prices and output as a market having perfect competition, whereas other assert the monopolistic tendencies of an oligopolistic market situation. The difficulty is how to determine oligopolies and which criteria that should be used when an undertaking participates in an oligopoly rather than being an individual company.

4.5 The tools of the Commission to handle oligopolies

Collective dominance is a concept used both under the Articles 81 and 82 and the Merger Regulation. There are several approaches to collective dominance, which make it difficult to establish a clear-cut definition since some differences arise depending on whether an economic or legal approach is used. The legal approach focuses on independence among the competitors and does not coincide with the economic approach that regards mainly market power. The concept of joint dominance matches closely the economic concept of co-ordinated effects, which can be thought to occur when a small number of large firms in a market, that is oligopoly, are able to co-ordinate their actions and maintain prices above the competitive level. The co-ordination does not need to be explicit, hence the practice is also referred to as “tacit collusion”. A major difference between the legal and the economic approach is

[17] Whish, supra note 16, pp 386-387.

that tacit co-ordination is not illegal, even if it economically give rise to the same anti-competitive effects as co-operation and concerted practice between companies, that is cartel behaviour. In oligopolistic market these effects often occur without any co-operation between the actors. In order to achieve successful tacit co-ordination it requires not only the ability to adopt a common level for prices or output, but also that some punishment strategy is available in order to prevent cheating.[19]

4.6 When can the concept of collective dominance be applied?

The recent extensive application of the concept by the Commission shows that even small companies may be embraced in a situation of collective dominance. For instance, in the Commission's decision Airtours/First Choice, the proposed merger was prohibited even though the parties had market shares as low as 21 per cent and 11% respectively.[20] The Commission concluded however that the impact of the merger would lead to an increased concentration and the post-merger combined market share of the three largest operators would be 83%. In addition to other characteristics of the market, the merger would have led to a collective dominant position for the parties.

The concept of collective dominance <u>under the Merger Regulation</u> can only be applied earlier to a declaration of compatibility of the concentration. Once a merger is declared compatible with the common market, the only remaining instruments to prevent undertakings on oligopolistic markets from abusing their positions are either Article 81 concerning concerted practice or Article 82 on abuse of a collectively hold dominant position. These situations are delicate to establish and the Commission has a considerable burden of proof, in particular as far as concerted practice is concerned, since it is very close to parallel conduct, which is legal. The preventative tool gained by the Commission when adopting the concept of collective dominance under the Merger Regulation is therefore a very welcomed remedy in order to protect an undistorted competitive environment from harmful oligopolies.

4.7 Collective dominance under Article 82

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[18] Hildebrand, Doris, The Role of Economic Analysis in the EC Competition Rules (1998), at p 101

[19] Caffarra and Kühn [1999] 7 ECLR pp 355-359

[20] Commission Decision Airtours/First Choice, No IV/M.1524 of 22.09.1999, para 72. The Commission's own estimation of market shares.

In Hoffman-La Roche in 1976 the Court held that oligopolistic but non-collusive parallel behaviour fell outside the scope of Article 86 (now Article 82): "[A] dominant position must also be distinguished from parallel courses of conduct which are peculiar to oligopolies in that in an oligopoly the course of conduct interact, while in the case of an undertaking occupying a dominant position the conduct of the undertaking which deprives profits from that position is to a great extent determined unilaterally."[21] However, in the Italian Flat Glass decision the concept of collective dominance was applied for the first time by the Commission and later confirmed by the Court. The provision under Article 82 was applicable since the undertakings were in a situation of interdependence and acted on the market as one single entity and not as individuals, jointed together by special links regarding the production. The Court held that the situation could be characterised by: "…two or more independent undertakings jointly have, through agreements or licences, a technological lead affording them the power to behave to an appreciable extent independently of their competitors, their customers and ultimately their consumers."

5. Case law on collective dominance under the Merger Regulation

5.1 Nestlé/Perrier – the Commission's first decision on collective dominance under the Merger Regulation

The Commission applied for the first time the concept of collective dominance under the Merger Regulation in the decision Nestlé/Perrier[22] in 1992. The Commission thoroughly examined whether the proposed merger would create an anti-competitive duopoly together with the competitor BSN. In this case the Commission held that Article 2(3) is not confined to situations where the dominant position is created or strengthened by a single firm, but it is also applicable in cases of " two or more undertakings holding the power to behave together to an appreciable extent independently on the market".[23] Before the merger there were only three operators in the oligopolistic market; Nestlé, Perrier and BSN. Nestlé undertook to sell the Perrier brand Volvic to BSN, since the Nestlé/Perrier independently would reach the threshold to a prohibition (single dominant position) if Volvic were kept in their

[21] C-85/76, Hoffman-La Roche v. Commission [1979] ECR 461, para 39
[22] Nestlé/Perrier, see supra note 12.
[23] See supra note 12, at para 114.

possession. However, the Commission found that a divesture of that brand would not help to clear the merger.

Price competition was weak with a high degree of price parallelism and a very high production cost margin. There were also high entry barriers due to a limited number of water springs. After the merger, the degree of concentration would be extremely high in the market in question,[24] since the merging undertakings would hold nearly 95 per cent of all still mineral water. The concentration would make anti-competitive parallel behaviour entailing collective abuse due to the transparency in the market, which facilitates tacit collusion as well as the possibility to monitor such collusion. The mineral water suppliers in France had developed instruments of transparency facilitating a tacit co-ordination of pricing policies. Moreover, the companies had developed instruments allowing them to control and monitor each other's behaviour.[25] The transparency in itself had a double purpose; to facilitate tacit collusion and to monitor that collusion. The Commission concluded on the basis of the above mentioned facts that the market structure resulting from the merger would create a duopolistic dominant position that would significantly impede the competition. Finally, the Commission approved the merger after considerable divesting measures of the parties.

5.1.1 The development of the concept of collective dominance

The Commission's decision Nestlé/Perrier shows that EC merger control does cover oligopolistic dominant positions. This first merger case on oligopolistic dominance offers useful insights into the approach of the Commission on this issue. Due to high levels of concentration, the Commission examined a long list of structural factors to in order to assess whether the market was prone to the development of tacit collusion or, as it also was called in the decision, anti-competitive parallel behaviour. After Nestlé/Perrier it was clear that the Commission also would take into consideration the creation or reinforcement of oligopolistic or collective dominant positions. Whether the Merger Regulation could be applied to these situations had been subject of discussions in the pasts. At this time, it was not yet confirmed by the Court. In the absence of the Court's approval, the Commission had a prudent attitude to the application of the concept of collective dominance to mergers. In Alcatel/AEG

[24] The geographic market concerned was France.

Kabel[26], the Commission rejected a request from the German Federal Cartel Office asking the Commission to conclude that the concentration would give rise to oligopolistic dominance. From the outset, the Commission had earlier taken the view that the Merger Regulation does apply to oligopolistic dominance, even though no prohibitions or undertakings to the merging companies had been pronounced.[27] However, there were doubts whether, as a legal matter, oligopolistic dominance was covered by the scope of the Merger Regulation, notwithstanding that the Court of First Instance had ruled that collective dominance was covered by the meaning of Article 86 (now Article 82).

The first ruling on collective dominance under Article 82 was the judgment Italian Flat Glass[28] in 1992, where three Italian producers of flat glass had entered into certain agreements that the Commission found to infringe Article 85 (now Article 81). On the basis of essentially the same facts, the Commission also found collective dominance under Article 82. While accepting the notion of collective dominance, the CFI did not agree that the three companies had adopted the same conduct on the market and the Commission's decision was annulled on this point. The CFI ruled that: "[t]here is nothing, in principle, to prevent two or more independent economic entities from being, on a specific market, united by such economic links that, by virtue of that fact, together they hold a dominant position vis-à-vis the other operators on the same market. This could be the case, for example, where two or more independent undertakings jointly have, through agreements or licences a technological lead affording them the power to behave to an appreciable extent independently of their competitors, their customers and ultimately of their consumers"[29] (judgment of the Court in Hoffmann-La Roche, cited above, paragraphs 38 and 48). Even though the Court found that the Commission had not done enough to establish collective dominance in this case, the parallel application of Article 81 and 82 was confirmed. However, it was not sufficient to "recycle" the facts constituting an infringement of Article 81 and then deduct from these facts the finding of an agreement between the parties. Among other considerations, a finding of a dominant position presupposes

[25] Nestlé/Perrier, see supra note 12, at paras 121 and 122
[26] Case No/M.165-Alcatel/AEG Kabel of 18.12.1991.
[27] See, inter alia, Renault/Volvo Case IV/M.004, Aerospatiale/MBB Case IV/M.017, Alcatel/Telettra Case IV/M. 042, Tetra Pak/Alfa-Laval Case IV/M.068, Aerospatiale-Alénia/de Havilland Case IV/M.053, Thorn EMI/Virgin Music Case IV/M.202.
[28] Cases T-68, 77 and 78/89 Società Italiana Vetro SpA v. Commission.
[29] See note supra 28, at para 358

that the market in question has been defined. However, recycling is accepted as reconfirmed in Compagnie Maritime Belge.[30] The ECJ held that the Articles 81 and 82 could be applied to the same action. Concerning fines, these may be reduced when the articles are simultaneously used. Concerning collective dominance, the Court held that a dominant position may be hold by two or more economic entities legally independent of each other and within the scope of the provisions of Article 81, provided that they, from an economic point of view, present themselves or act together in a particular market as a collective entity. Whether the undertakings constitute a collective entity can be established by examining possible links. However, the Court held: "…the existence of an agreement or of other links is *not indispensable* to a finding of a collective dominant position; such a finding may be based on other connecting factors and would depend on an economic assessment and, in particular, on an assessment <u>of the structure of the market</u> in question"[31](my remark). This statement is very interesting, in particular the reference to the structure of the market as it gives rise to the question whether this description of collective dominance under Article 82 reconciles the case-law of oligopolistic dominance in merger cases.

5.2 Kali & Salz – the ECJ rules on the application of collective dominance in merger situations

In December 1993, the Commission declared the proposed merger between Kali & Salz AG and Mitteldeutsche Kali AG ("K&S/MdK") compatible with the common market, but only after the parties complied with the undertakings set out in the Commission's decision. The Commission held that the proposed transaction affected two relevant markets; Germany and the European Community (apart from Germany). In Germany, the merger gave rise to a position of single firm dominance on the German market for potash, a mineral fertiliser. However, despite a combined market share of 98 per cent, the Commission concluded that the "failing firm defence" could be applied and consequently the merger did not give rise to any serious concerns in that market. However, regarding the other market, the European Community (Germany excluded), the Commission argued that the proposed concentration would

[30] Joined cases C-395/96 and C-396/96P Compagnie Maritime Belge Transports and others v. Commission, 16.03.2000
[31] See supra note 30, at para 45

create a situation of oligopolistic dominance on the part of the merged entity and the French public-owned producer, Société Commerciale des Potasses et de l'Azote (SCPA). For this reason, the Commission required K&S to eliminate its links with SCPA, which was the main distributor of K&S's supplies in France, and their common participation in an export joint venture before permitting the merger. These undertakings did not please the parties and appeals were lodged against the decision both from K&S and from the French government on behalf of SCPA.

In March 1998, the ECJ delivered its Kali & Salz judgment on the appeals against the decision of the Commission[32]. The Court annulled the decision on the grounds that the Commission had not adequately established that an oligopolistic dominant position would be created or strengthened. This judgment has several important contributions for the application of European merger control with respect to oligopolistic dominance. First, Kali & Salz confirmed that the Merger Regulation could be applied to mergers which gave rise to positions of oligopolistic dominance. Legal concerns were raised regarding the lawfulness of the application of the Merger Regulation to the creation of more than one company before the Court's affirmation in Kali & Salz. Secondly, the judgment has an impact on the way in which the Commission conducts its economic appraisal of oligopolistic dominance in the future. Thirdly, the Court confirmed the concept of failing firm.[33] Also some procedural issues were raised in this case, concerning the scope of right to a hearing. Moreover, the new (second) decision by the Commission provides guidance concerning legal deadlines for a second decision. Another interesting issue resulting from this case is the possibility to damage for the parties concerned.[34] The Merger Regulation does not contain any provisions of this kind. The parties did not seek damages so unfortunately this matter was never discussed.

In the Kali & Salz judgment the Court accepted that the Commission enjoys considerable discretion in determining whether a concentration creates a risk of oligopolistic dominance. In particular, when assessing the concentration the Commission is not required to apply or rely on the criteria developed in prior cases.

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[32] Kali und Salz/MdK/Treuhand, IV/M.308 of 14.12.1993.

[33] For a detailed explanation see Monti and Rousseva, Failing Firms in the Framework of the EC Merger Control Regulation, (1999) 24 EL Rev at pp 38-55.

[34] Briefly discussed by Kent Karlsson and Fredrik Hägglund in ”Begreppen Failing Firm och Kollektiv Dominans” ERT 2 1999, at pp 21-43.

Nor is it bound by the jurisprudence developed under Article 82. For example, the Court did not expressly address the French Government's allegation that the Commission had incorrectly applied the concept of oligopolistic dominance because it had based its analysis on criteria that are not contained in the case law under Article 82.[35] Previous case-law on joint dominance under Article 82 has been complicated by the discussion of the relationship between the Articles 81 and 82 and the application of both articles to the same set of facts in, for example, Continental Can, Italian Flat Glass and now recently in Compagnie Maritime Belge. This flexible approach, which probably has been developed due to the complexity of the economic analysis, which the assessment of oligopolistic collusion requires, acknowledges the need for a case-by-case approach. As such, the Court's approach is consistent with the views expressed by many authors. As Kantzenbach writes: "[t]he implication for practical competition policy, especially the application of the European merger control, is that the factors inhibiting or encouraging collusion have to be determined on a case-by-case or sector-by-sector basis".[36] He also observes that there may exist some tension between this approach and the interests of legal certainty in which it could lead to a conflict with the overall requirement that competition policy should be oriented to clear decision-making rules in order to ensure security to the planning of the companies. The Court seems to have ruled in favour of the flexibility required by the complex economic analysis.

The Commission had applied the Merger Regulation on a significant number of decisions, where there was an element of collective dominance, despite lack of legal justification. Since the wording of the Regulation does not explicitly include a situation of collective dominance, the Commission made this interpretation. In the Kali & Salz-judgment the Court finally confirmed the practice of the Commission by declaring the Merger Regulation applicable on situations of collectively held dominance. In 1999, this position was reconfirmed by the Court in the judgment Gencor v. Commission.

[35] See supra note 10, at para 179.
[36] Kantzenbach, Kottham and Kruger, New Industrial Economics and Experiences from European Merger Control – New Lessons about Collective Dominance? (1995), page 3-4.

5.2 1 Legal aspects raised in Kali & Salz

Although, it was general consensus among economists that oligopolistic dominance was an issue that should dealt with under the merger control[37], there were doubts as to whether as a legal matter oligopolistic dominance fell within the scope of the Merger Regulation. These concerns were particularly dealt with in the Advocate General Teasaro's opinion, while the Court found that the Merger Regulation could be applied to this type of dominance. The Court reaffirmed its teleological approach and relied on earlier judgments such as Continental Can[38] and BAT and Reynolds[39] where it had relied on fundamental goals embodied in Article 3(g) of the Treaty in order to avoid a lacuna in Community law. The Court started to acknowledge that there was no definitive textual evidence whether the Merger Regulation applies to oligopolistic dominance. In particular, the choice of legal bases for the Merger Regulation and the wording of article 2 and its legislative history are all inconclusive on this point. Against this background, the Court cited Netherlands v. Commission[40] and held that since the legal basis, text and legislative history of the Merger Regulation do not provide an answer as to whether it applies to oligopolistic dominance, it is necessary to interpret Article 2 teleologically by reference to its purpose and its general structure. Concerning the application of this approach, the Court then concluded that, given the recitals to the Merger Regulation, particularly the 1st, 2nd, 6th, 7th, 10th and 11th recitals, the Merger Regulation was intended to apply to concentrations insofar as they are likely, because of their effect on the structure of competition within the Community, to prove incompatible with the system of undistorted competition envisaged by the Treaty. According to the Court, to find otherwise would be partly to frustrate the purpose of the Merger Regulation. The Advocate General also invoked the 15th recital, which prescribes that concentrations are in principle compatible with the common market if the undertakings concerned have a combined market share of less then 25 per cent would mean that the Merger Regulation only could be applied to single firm dominance. In the Court's view that recital could not be relied on in order to establish the non-applicability of the Merger Regulation to oligopolistic dominance. According to the Court, the presumption of that recital was not developed in any way in the operative part of the Merger Regulation.

[37] See for example Winckler and Hansen, (1993) Common Market Law Review 30: 787-828.
[38] Case 6/72 Continental Can
[39] Case 142 & 156/84 BAT and Reynolds

Collective dominance in Article 82 situations did not raise the same legal concerns as the application of the concept under the Merger Regulation. The preparatory work of the Regulation shows that the Member States represented in the Council did not agree on the question of control of oligopolies.[41] However, the ECJ considered that neither the legal basis of the Merger Regulation, nor the wording of its Article 2 excluded its application to oligopolies. According to previous jurisprudence,[42] the preparatory works of an EC legal measure are of no assistance for its interpretation. The Court adopted, in Kali & Salz, a teleological approach and based its argumentation on the recitals in the preamble to the Regulation, in particular, recital 6 which refers to the legal lacunae left by Article 81 and 82 EC, and recital 7 regarding the purpose to control "all operations which may prove to be incompatible with the system of undistorted competition". Indeed, there would have been a lacuna in the EC competition policy if oligopolistic markets were left aside. The Court also referred to the objective of competition policy; that is, ensuring that the competition in the common market is not distorted. This would have been frustrated if the Merger Regulation did not apply to oligopolies. This approval of the concept of collective dominance by the Court has given confidence both to the Commission and to the national authorities in applying the theory of collective dominance in merger cases. Legally this interpretation of the Merger Regulation does not seem to be very controversial and the issue has not been raised in any later decisions or judgments. The legal concerns that can be raised regard rather the scope of collective dominance and consequently also the problem of unpredictability.

5.3 Gencor v. Commission – the CFI rules on the importance of links

The judgment from the CFI on Gencor's appeal against the Commission's prohibition of the Gencor/Lonrho merger[43] provides clarification on some issues and has already become a standard reference. In Gencor v. Commission[44] the CFI upheld the decision by the Commission on all points raised by the applicant. The judgment concerns several delicate matters of the scope of the Merger Regulation, inter alia the

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[40] Case 11/76 Netherlands v. Commission.

[41] Garcia Pérez, Mercedes, Collective Dominance under the Merger Regulation, (1998) 23 ELRev at pp. 475-480.

[42] Case 15/60 Simon v. Court of Justice, at para 167.

[43] Case No IV/M.619 Gencor/Lonrho of 24.04.1996.

[44] See supra note 11.

jurisdiction and the interpretation of evidence. The creation of a joint venture between the two firms would have created a collective dominant position for the new entity and a third party and thereby reduced the number of companies controlling the platinum reserves in South Africa from three to two. These reserves were estimated to count for nearly 90 per cent of the world known reserves of platinum. The merger would have reduced asymmetries between the companies, which is generally considered rendering co-ordination less difficult. The Commission also pointed out that by bringing together a high-cost producer and a low-cost producer would result in an elimination of asymmetries in costs between the two firms. Together with a considerable fragmentation of marginal supplies this was likely to increase the joint dominance as a result of the merger. The Court concluded that the concentration would have had the direct and immediate effect of creating the condition in which abuse was not only possible but also economically rational, given the structure of the market.[45] With only two firms having broadly similar cost structures, an anti-competitive parallel conduct would, economically, have constituted a more rational strategy than competing with each other, thereby adversely affecting the prospect of maximising combined profits.[46] The Commission emphasised the importance of a thorough economic investigation in order to find what factors in oligopolistic markets that are typically facilitating co-ordination. Among these we find inter alia: high concentration levels, stable and symmetric market shares, similarity of cost structures, stagnant and inelastic demand, homogeneous products, and low levels of technological change.

The major contribution of the judgment concerns the explicit acknowledgement of joint dominance with the economic concept to tacit collusion. The importance of links between firms was reduced to a relevant but not necessary criterion. The Court clarified that explicit collusion will have to be dealt with under Articles 81 and 82. The focus of merger control shall instead be on whether the merger will increase the feasibility of co-ordination or tacit collusion. This is of great legal importance, while economically no meaningful distinction can be drawn for the purposes of prevention between explicit and tacit collusion.

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[45] See supra note 11, at para 94
[46] See supra note 11, at para 236

6. Assessment of oligopolistic dominance

6.1 Introduction

In cases of merger in the context of single dominance, the Commission usually analyses whether remaining, actual or potential, competitors are able to constitute a sufficient competitive constraint on the leading supplier. The perspective of merger investigation in cases of oligopolistic dominance is necessarily considered to be different since the members of the oligopoly are by assumption capable of exerting such a constraint on each other. The first question to be answered is, therefore, whether the post-merger market structure is such that, given the interdependence between the members of the oligopoly, the companies would be able to maximise their profits jointly by avoiding competition amongst themselves. Oligopolists will sooner or later find a way of avoiding competition among themselves, since they are aware that their overall profits are maximised with this strategy. However, the question is much more complex. First of all, collusion without explicit agreements is not easy to achieve or to establish, since there will not be any written agreements to enforce against a company that deviates from the common strategy. Each supplier might have different views on the level of prices on which the demand will sustain or may have different price preferences depending on their cost conditions and market shares. Moreover, if tacit collusive strategies are implemented and oligopolists manage to raise prices significantly above their competitive level, each oligopolist will be confronted with a conflict between sticking to the tacitly agreed behaviour or to increase its individual profits by cheating on its competitors. Consequently, the key issue for the Commission is to find out how likely or how easy it will be for oligopolists to collude or avoid competition among themselves after the merger.[47]

The first step of the analysis consists of establishing whether the post-merger market structure will induce the leading firms to engage in anti-competitive parallel behaviour as to attain a level of profit reminding of that of a single dominant firm. Therefore, the transparency of the market will be examined thoroughly. In a second step, the Commission establishes whether the remaining competitors are able to constitute a sufficient competitive constraint on the members of the oligopoly. The conditions of the demand and price elasticity play an important role in the analysis.

[47] Briones (1993), see supra note 14, at p. 119.

As for all competition assessment, the definition of the relevant, product and geographic, markets constitute the first step in the analysis.

6.2 Criteria for assessing collective dominance

It is unlikely that there will be a risk of oligopolistic dominance in the absence of structural factors. In this category of market features the degree of concentration, barriers to entry or exit and demand side factors are of significance in the assessment. These are necessary but not sufficient for a finding of oligopolistic dominance.

6.2.1 The role of market definition and concentration measures

A high degree of concentration will increase the risk of collusion in the relevant market.[48] The market definitions permits the calculation of market shares and consequently allows the impact of the market concentration to be statistically summarised in measures such as the Herfindahl-Hirschman Index (HHI). The impact of a merger on concentration is a relevant consideration when assessing whether the merger is likely to result in co-ordinated effects. The degree of concentration gives an indication of how likely it will be for the remaining firms to agree on collusive agreements. The importance of the concentration criterion has been confirmed by the game-theory analysis.[49]

6.2.2 Degree of concentration

Does the merger materially increase concentration? A reduced number of firms, each with increased market shares, are more likely to spot cheating and have less incentive to cheat as well as are more likely to get caught cheating. Furthermore, it is easier to sustain collusion with many small buyers rather than a few large ones. Concentration is an important factor since large actors are more likely to be detected if they cheat than small ones. Large players are also more likely to detect the cheating of others because they have information about the market in its capacity of being a major part of it. In addition, fears of collusive activity are confined to industries in which the products are relatively homogenous, with little differentiation or customisation. This is due to the fact that it is easier to fix a schedule of collusive prices when products are similar than when they all have different characteristics and when sales at very different prices and can be modified for specific customer needs. For these reasons,

[48] Kantzenbach, Kottham and Kruger, supra note 35, at p 8.

concentration in the assessment of co-ordinated effects and the standard measures of it, such as HHI, provide important information about the market. The Commission examines the concentration in depth, where high combined market shares in combination with other factors are present. In cases where it has only been two companies in the market, the Commission has initiated investigations about collective dominance at combined market shares above 50 %. The Commission has tended to focus almost exclusively on duopolies with high combined market shares,[50] in recognition of the fact that collusion becomes more difficult to sustain as the number of member in the oligopoly increases. It seems not to be a fixed limit of how many undertakings that can be part of an oligopolistic dominant position.[51] However, other factors may mitigate the risk of a creation an oligopolistic market structure. For example, in Knorr-Bremse/Allied Signal[52], the Commission approved a concentration with duopoly shares of 80 per cent because of countervailing factors such as a highly concentrated demand side, the existence of potential competition and steady decline in the parties' market shares. Similarly, in Knorr-Bremse/Bosch[53], the Commission concluded that although there would be more or less two equal players with a market share over 75 per cent after the merger, co-ordinated behaviour would be difficult to achieve given the countervailing purchasing power, potential entry, the significance of innovation, lack of transparency and the importance of non-price criteria. The last criterion implies that competition is present on other factors than just price, which makes the market less transparent and thereby also complicates collusion.

When the market consists of four to six suppliers, the Commission has previously examined the outcome of the merger at market shares of 80-90 %. However, this guidance is no longer reliable. Other factors have appeared to be equally important and in the decision Airtours/First Choice the Commission blocked the merger where previously four suppliers would have been reduced to three having combined market shares of only 51 per cent. In principle, collective dominance is unlikely to occur

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[49] Kantzenbach, Kottham and Kruger, supra note 35, at p 10.
[50] See e.g. Nestlé/Perrier, see note supra 12, where the two parties had a combined market share of 82 per cent.
[51] See for example Case No IV/M.358 Pilkington-Techint/SIV of 21.12.1993, Case No IV/M.523 Akzo Nobel/Monsanto of 19.01.1995, Case No IV/M.1016 Price Waterhouse/Coopers&Lybrand of 20.05.1998 and Case No IV/M.1524 Airtours/First Choice of 22.09.1999. In the last decision, the Comomission blockad for the frist time a merger which gave riste to an oligopolistic dominance containing more than two undertakings.
[52] Case No IV/M.337 Knorr Bremse /Allied Signal of 15.10.1993.
[53] Case No IV/M.1342 Knorr-Bremse/Bosch of 14.12.1998.

between more than four suppliers, since tacit collusion would probably not be stable in long term considering the principles of oligopolistic theory.

In Price Waterhouse/Coopers & Lybrand the Commission noted that as far as single dominance was concerned, the outcome of the 'Big Six' competitive bidding activities over a period of years would be a sufficient constraint by the competitive behaviour of the remaining four large accounting firms. [54] Regarding collective dominance the situation was more complicated and the Commission found that the market in question was characterised by many elements conducive to the creation of such dominance; demand was not fast growing and is relatively insensitive to price and the service is homogeneous. Furthermore, the market was rather transparent and characterised by a low rate of innovation. The suppliers were interlinked via self-regulatory professional organisations and clients tended to be "locked in" to incumbent auditors for long periods because of significant switching costs. Despite these market characteristics, the Commission found no conclusive proof showing that the merger would create or strengthen a position of collective dominance within any of the national Large Company/"Big Six" markets for audit and accounting services within the European Union. In view of the continued post-merger existence of no fewer than five suppliers, the likelihood of continued participation of these five suppliers in the tender offers which constitute the competitive process in the relevant market, the non-emergence of two clear leading firms post-merger and in general the improbability that a situation of collective dominance at the level of five service providers would be stable over time, persuaded the Commission to clear the merger.

Although the emphasis of Article 2 (1) (a) of the Merger Regulation clearly focuses on the market structure, market shares are still regarded as a crucial criterion. The Merger Regulation does not specify a minimum market share from which a threat to competition is perceived. However, an indication is given in recital 15 of the preamble to the Merger Regulation.

"Whereas concentrations, which, by reason of the limited market share of the undertaking concerned, are not liable to impede effective competition may be presumed to be compatible with the common market; whereas without prejudice to

[54] Case No IV/M.1016 Price Waterhouse/Coopers & Lybrand of 20.05.1998, at para 103.

Article 81 and 82 to the Treaty, an indication to this effect exists, in particular, where the market share of the undertakings concerned do not exceed 25 per cent either in the common market or in a substantial part of it."[55]

These few lines from the Commission concern merger control in general, with or without risk of oligopolistic dominance. However, after the Commission's decision in Airtours/First Choice, where the Commission stretched the concept even further and applied it to the two the merging parties holding 21 and 11 per cent of the market respectively, there seems not to be a minimum percentage of market shares as far as joint dominance is concerned. The recital 15 of the preamble has no longer any actual relevance, since the Commission more and more often uses the concept of collective dominance with cumulated market shares. The assessment of the Commission focuses on how the post-merger market will facilitate or obstruct co-ordination of strategies between the remaining competitors. This criterion is surrounded by doubts. It implies a thorough market investigation and an analysis of economic theory. In addition, there are uncertainties about which economic theory that shall apply. It seems like the New Industrial Economic Organisation Theory prevails, which is focused on the market structure. From a lawyer's point of view, the element of economic theory has made the merger control more legally unpredictable.

The risk of parallel conduct will decrease by natural reasons if the alleged oligopoly consists of more than two companies. An interesting question regards the number of companies that can be part of an alleged oligopoly and hence be object to a prohibition of a notified merger. In Airtours/First Choice, three companies were for the first time involved in a joint dominant position. In Price Waterhouse/Coopers & Lybrand, the Commission indicated an upper limit and the Commission held that: "…a dominant position, hold collectively by more than three or four suppliers, is too complex and unstable to be persistent over time".

Accordingly, the Commission will probably not interfere if the alleged oligopoly consists of at least five companies, since such a construction is deemed too unstable to persist over time and hence the risk of anti-competitive parallel behaviour is judges

[55] Recital 15 of the preamble of the Merger Regulation.

to be too insignificant. In the decision ENSO/Stora[56], the Commission held that a necessary, but not sufficient, criterion for interference is that the companies concerned, no matter if they are two, three or four, collectively are in position of such market power that characterises collective dominance.[57]

In other cases, the Commission has found that high market shares can be outweighed by strong competition, which will prevent collusion.[58]

There are other factors which need to be considered when looking at the likelihood of collective dominance, but an initial appraisal based on concentration and concentration changes is likely to provide a reliable foundation for the subsequent analysis.

6.2.3 Product Homogeneity

Is the product relatively homogeneous? Product homogeneity makes collusive outcomes easier to sustain or achieve. A market with homogeneous products makes it easier to compare prices and accordingly it is easier to reach a common price level. If the product is homogeneous, without quality differences, the only competitive aspect may be the price. An example of such a product is fuel. Moreover, in a homogeneous market deviations from a tacitly agreed price will be easier to detect, which makes it more difficult for oligopolists to cheat. In Gencor/Lonrho the product concerned, platinum, was indeed a homogeneous product. So was also recognised in Nestlé/Perrier, where the Commission refused to believe in brand differentiation on bottled still water, as well as in Thorn EMI/Virgin.[59] Products can be standardised because of regulatory requirements, such as auditing services, which was the case in Price Waterhouse/Coopers & Lybrand.[60] However, competition may take place on other factors than on price, like quality, service and competence, which have been taken into account in several decisions, for instance, Knorr-Bremse/Allied Signal.[61]

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[56] Case No IV/M.1225 Enso/Stora of 25.11.1998.
[57] EnsoStora, press release IP/98/1022.
[58] See inter alia Case No IV/M.186 Henkel/Nobel of 23.02.1992 and Airtours/First Choice, supra note 20 .
[59] See Nestlé/Perrier supra note 12 , at para 22; Case No IV/M.202 Thorn EMI/Virgin Music of 12.05.1992, at para 29.
[60] See supra note 54, at para 100.
[61] See supra note 53,at para 33.

6.2.4 Price elasticity

If competition mainly is based on price, extensive non-price competition may entail that even agreement on prices does not prevent collusion-breaking competition between firms. The lack of price-elasticity was cited in Nestlé/Perrier indicating that collusion could successfully occur.[62] In a price-inelastic market, the competitors are more likely to raise prices as a result of tacit collusion, since there is a less significant risk of losing sales. Price inelasticity is most likely to occur in a mature market, where there is a small degree of innovations. This aspect is also related to product homogeneity, since markets tend to become more and more homogeneous over time. Also the degree of innovation will often reach a point of exhaustion. In Gencor/Lonrho the maturity of existing mining and refining technologies in combination with the fact that innovations were unlikely, increased the fear that the parties would engage in parallel behaviour.[63]

6.2.5 Transparency

Are prices transparent to competitors? Transparent pricing makes cheating easier to detect and thereby deters stable collusion. Price comparisons are also facilitated by factors like product homogeneity and a low degree of innovation, since the latter leads to product differentiation. A certain degree of transparency enables the competitors to get access to information on price on volumes of the other suppliers, which makes monitoring of parallel behaviour possible. The market is naturally transparent if factors like few suppliers and little price differentiation is at hand. In Gencor/Lonrho, both price and volume were transparent, since all trading was made through stock exchange, statistics on production was regularly published and the sales contract on the markets contained a clause that prohibited resale of platinum.[64]

6.2.6 Stable demand and excess capacity

Is demand stable? It is harder to spot cheating in markets which are rapidly growing and so collusion is less likely in an expanding market. Demand often becomes stable in mature markets. If the demand is declining, excess capacity is likely to occur, which can have an ambiguous effect on collusion. On one hand it is more likely that the oligopolists will engage in tacit collusion to maintain price at a supra-competitive

[62] See supra note 12,at para 124
[63] See supra note 43, at para 152
[64] See supra note 43, at para 144-145

level. This is most likely to occur if there is excess capacity on the whole market. On the other hand, excess capacity may provide an incentive to compete and limit the ability to discipline each other on collusion, since it may be attractive to gain a larger profit by gaining market shares.

6.2.7 Symmetrical market positions

If the remaining players are of similar size and with a similar cost structure, differences in cost structures or size may give firms different incentives to cut prices making the collusion less stable. It is generally recognised by industrial economists that the significant symmetries will increase the likelihood of collusion or conscious parallelism since asymmetries are likely to give rise to conflicting interests.[65] In the assessment of Enso/Stora, the Commission noted that in this case, similar cost structures was one of the most important indications of the likelihood of the parties to engage in parallel behaviour.[66] Similarities may be expressed in similar size of the companies and the market shares. This was the case in Gencor/Lonrho, where the duopoly would attain a market share of 30-35 per cent each and together would control 90 per cent of the world reserves of platinum. The similarities would reduce the incentive to compete. A consequence of symmetries is that a potential price increase would have the same effect of both companies and thus they would have a common interest to behave in the same way, which makes parallel behaviour highly accessible.

It is also of interest to investigate if the acquired firm was a maverick. If the acquired firm was noted for being particularly aggressive in its response to competition its loss may make collusion much more likely once it has disappeared. On the other hand, concerns will be mitigated if remaining marginal competitors can offer a sufficient competitive constraint. This will subsequently disturb any attempt to collude.

6.2.8 History of cartelisation

Is there a history of explicit attempts at cartelisation in the market? Markets with history of cartel behaviour are likely to be susceptible to co-operation. Cartel relations between suppliers or an industry prone to tacit collusion will increase the concerns of

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[65] Kantzenbach, Kottham and Kruger, note supra 35, at p 58.
[66] See supra note 56, at para 67.

parallel behaviour also in the future. This was noted in Glaverbel/PPG[67], where two float glass suppliers notified a concentration. In another merger, but related to the same industry, glass production, this was equally taken into account, though both mergers were cleared.[68] Also in Nestlé and Gencor past parallel pricing was considered and taken into account as an indicator of future collusion.

6.2.9 Vertical integration

The degree of integration in the upstream and the downstream market may affect the supplier's willingness to engage in parallel behaviour. Thorough investigations on this point have been made in Mannesmann/Vallourec/Ilva[69] and now recently in Airtours/First Choice. For example downstream vertical integration might affect the market transparency, which will have an influence on the likelihood of successful parallel pricing.

6.2.10 Links

In Gencor v. Commission, the CFI has clarified that there is no need for oligopolists to be interrelated by any specific links in order to establish collective dominance. This ruling offers an extensive interpretation of links in the context of collective dominance. The Commission took into account any structural links between the parties concerned and third parties within the same sector of activity, even though such links did not mean that the parties had control, in the meaning of Article 3 of the Merger Regulation, over such third parties. Not only structural, but also economic and other links tended to give rise to doubts as to the compatibility of the operation.[70]

6.2.10.1 Structural links

The existence and the importance of links between the merging companies and third companies susceptible of detaining a collective dominant position have during a long time been surrounded by uncertainty, but it now seems like the situation has been clarified to some extent. According to recent case law, links shall rather be regarded as an indication among others of collective dominance, but neither as a necessary nor sufficient criterion. The term link is abstract and may cover a wide number of issues, whose importance range from insignificant to crucial. The relevance and importance

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[67] See Case No IV/M.1230 Glaverbel/PPG of 07.08.1998 at para 20.
[68] See Pilkington-Techint/SIV, supra note 51, at para 76.
[69] See Case No IV/M.315 Mannesmann/Vallourec/Ilka of 31.01.1994, at para 55.

of links depend on the specific nature of the link and of the context of the case. In Kali & Salz the Court rejected the significance of the structural links, so prominently relied on by the Commission in its decision Kali & Salz. The Court held that the Commission had not adequately established the alleged links. This indicates that the presence of structural links is not sufficient to create a risk of oligopolistic dominance. The Court's judgment did not address the issue of whether structural links are necessary for finding of oligopolistic dominance. The Court ruled that the Commission should analyse if the concentration "…leads to a situation in which effective competition is significantly impeded by the undertakings involved in the concentration and one or more undertakings which together, *in particular* because of factors giving rise to a connection between them, are able to adopt a common policy on the market and to act independently of other competitors, their customers and also of consumers."[71] The reference to links was prefaced by the words "in particular" and therefore the situation was not clearly assessed and opened up for diversified interpretations. Moreover, the Court did not define the correlative factors, even though it could be interpreted from the judgment it concerned factors, which would facilitate for the parties to engage in parallel behaviour. Kali & Sal was perhaps not the most appropriate case for an assessment of the importance of structural links, since already the joint market shares held by Kali & Sal and SCPA was judged too inferior, in the context of other relevant factors, to create a collective dominant position. However, the emphasis placed by the Court on interdependence indicates that structural links were probably not even a necessary criterion.

The significance of links was further dealt with in the judgment Gencor v. Commission. The CFI held that the Commission might restrain a concentration leading to collective dominance, whether there are links or not between the two surviving firms. Gencor v. Commission was an appeal to the CFI from the decision of the Commission. The Commission considered a joint venture between two South African producers incompatible with the common market. The concentration would bring closer two rhodium and platinum mines and would have led to a dominant duopolistic position holding 80 per cent of the market shares of platinum worldwide. The CFI, which agreed with the Commission on all points raised by the plaintiff, found that the Commission had based its decision of joint dominance on various

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[70] XXIVth Report on Competition Policy, at p 299.

considerations, especially high entry barriers and large market shares. Moreover, the joint venture and its major competitor had similar cost structures with high overheads[72]. The products were homogenous and the prices transparent[73]. Other suppliers would have problems to face the economic power of the duopoly. The CFI concluded that structural links were no longer necessary in order to establish collective dominance[74]. The notion of links, stated in earlier case law, may arise not only from structural factors but also, as the CFI concluded, that a position of dependence between suppliers in a tightly concentrated market may amount to a relevant link. The CFI referred to Italian Flat Glass, in which it ruled in 1992 that "… there is nothing, in principle, to prevent two or more independent economic entities from being united by economic links in a specific market and, by virtue of fact, from together holding a dominant position vis-à-vis the other operators on the same market (…) where two or more independent undertakings jointly had, thorough agreements or licences, a technological lead affording them the power to behave to an appreciable extent independently of their competitors, their customers and, ultimately, of consumers."[75] However, in Gencor v. Commission the Court stated: "In its judgment in the Flat Glass case, the Court referred to links of structural nature *only by way of example* (emphasis added) and did not lay down that such links must exist in order for a finding of collective dominance to be made"[76]. It now seems like the importance of links has been reduced to the role of an example of a factor that may amount to collective dominance. An interesting issue at this time was whether this reduced importance of links also concerned the assessment of collective dominance under Article 82. The CFI referred to Italian Flat Glass, which was a case that concerned the applicability of the concept of collective dominance under Article 86 (new 82). In March 2000, the Court delivered its judgment Compagnie Maritime Belge[77], concerning both Articles 81 and 82. The Court ruled that links are not required for a finding of collective dominance under Article 82. These rulings of the CFI and the Court seem to be compatible with economic theory, which does not consider links of decisive importance for parallel behaviour in oligopolistic markets.

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[71] See supra note 10, at para 221
[72] See supra note 11, at paras 218-222.
[73] See supra note 11, at paras 226-230.
[74] See supra note 11, at paras 273-284.
[75] See supra note 28, at para 258.
[76] See supra note 11, at para 273.
[77] C-395 and 396/96 Compagnie Maritime Belge Transports v. Commission

Nevertheless, where present, structural links and mutual commitments can, in an appropriate case, be significant factors enhancing the likelihood of collusion. Certain categories of links require a particular assessment because they may affect the transparency of the market or otherwise reinforce the likelihood of parallel behaviour. Such links may be particularly important because they compensate for the lack of natural transparency in market conditions. Links may take different forms, including repetitive contacts between the same players, which tend to reduce the uncertainty and enable them to gain a better understanding of each other's competitive strategies. Links between customers and their suppliers may also increase the risk of collusion because they tend to create dependency between the customer and supplier.[78] Relations between different suppliers on oligopolistic markets may also increase the transparency. Such links were examined in Pilkington-Techint/SIV[79] where the commission found that cross-supply relationships reduce information gaps, since the buyer can compare the prices charged by the suppliers, although it also noted that the cross supply relationship was justified on efficiency grounds.

The Court does no distinction between economic and structural links, as ruled in paragraph 275 of Gencor v. Commission: "nor can it be deduced (…) that the Court has restricted the notion of economic links to the notion of structural links...".Furthermore, there is no reason whatsoever in legal or economic terms to exclude from the notion of economic links the relationship of interdependence existing between the parties to a tight oligopoly within which, in a market with the appropriate characteristics, in particular in terms of market concentration, transparency and product homogeneity, those parties are in a position to anticipate one another's behaviour and are therefore strongly encouraged to align their conduct in the market, in particular in such a way as to maximise their joint profits by restricting production with a view to increase prices. In such context, each trader is aware that highly competitive action on its part designed to increase its market share (for example a price cut) would provoke identical action by the others, so that it would derive no benefit from its initiative."[80]

"That conclusion is all the more pertinent, with regard to the control of

[78] Venit, James S, Two Steps Forward and No Steps Back: Economic Analysis and Oligopolistic Dominance after Kali & Salz, CMLRev [1998], at p 1133.
[79] See supra note 51, at para 39.

concentrations, whose objective is to prevent anti-competitive market structures from arising or being strengthened. Those structures may result from the existence of economic links (…) or from market structures of an oligopolistic kind where each undertaking may become aware of a common interest and, in particular, cause prices to increase without having to enter into an agreement or resort to a concerted practice".[81]

This market structure is a result of the particular situation on an oligpolistic market. On these grounds a merger can be prohibited before the creation of a situation of joint dominance. The reasoning seems to be that it is better to prevent a situation of harmful market structure then trying to correct a situation where the companies have abused their position on the market. Establishing abuse of collective dominance according to Article 82 or concerted practice in Article 81 demands convincing proof. A pre-examination is easier to prove and from legal aspects more sound and also the only efficient way to deal with oligopolies.

6.2.10.2 Ownership links

Ownership links are another type of structural link that may facilitate collusion. In the Commission's decision Gencor/Lonrho, the concentration was prohibited since the cross holding of a joint venture between the parties would result in a collective dominant position for the parties. In Kali & Salz, the structural links consisted of (i) the control of a joint venture in Canada, (ii) co-operation in the export cartel, Kali-Export GmbH, co-ordinating the members, sales of potash to non-member countries and in which Kali & Salz had essential interest (iii) long established links on the basis of which SCPA distributed almost all of Kali & Salz's supplies in France. These were invoked by the Commission together with other factors, for example, the degree of concentration in the market and the characteristics of the product resulting in collective dominance for the parties. However, the Court did not find the analysis on any of these points persuasive and rejected, in particular, the Commission's arguments regarding "structural links". The Court concluded that the Commission had not "on any view established to the necessary legal standard that the concentration give rise to a collective dominant position.[82] Since analysis in this area

[80] See supra note 11, at para 276.
[81] See supra note 11, at para 277.
[82] See supra note 10, at para 249.

often is difficult, the Commission must in the future make a greater effort to market evidence to establish any perceived co-ordinated effects of a merger.

6.2.10.3 The appraisal of joint ventures

Problems arise since the term joint venture involves different degrees of co-operation; from simple research projects to operations that reminds more of a concentration than of co-operation. The Commission’s policy is that where parents of a joint venture retain significant activities in the same market as their joint venture, this will almost invariably lead to co-ordination of competitive behaviour in a way that is likely to restrict competition. The existence of joint ventures between members of an oligopoly might facilitate the mutual monitoring of production and/or commercial policies of the parents. This depends on the arrangements entered into by the parents of the joint venture. In the Italian Flat Glass decision the two companies concerned had a pure production joint venture, which represented a negligible part of the sales on the relevant market. Furthermore it had no marketing of its own and sold only its output to the parents in equal shares. Under these arrangements the Commission concluded that the operation of the joint venture did not allow the parents to gain a thorough knowledge of each other’s production plans or pricing and marketing policies. The analysis seems to be similar under the Merger Regulation. However, in the context of other factors, a joint-venture may enhance the risk of collusion after the merger, as in Gencor v. Commission.

6.2.11 Barriers to enter and to exit the market

High barriers to enter the market was found, inter alia, in Nestlé/Perrier and Gencor/Lonrho. The Commission held that oligopolists controlled all the major reserves of spring water respectively platinum. In Gencor the Commission also noted that the industry was very capital intensive and that sunk costs were high.[83] In Nestlé/Perrier the Commission found that the market was stagnant and technologically satirised. There was also high brand-consciousness among the consumers in combination with important advertising costs. These factors reduced the likelihood of new competitors on the market, which meant that the market was not likely to be less concentrated in the future.

6.3 A case study of the Commission's decision Airtours/First Choice

In 1999, Airtours announced its intention to acquire First Choice by way of public bid. Both companies were operating on the market for short-haul package tour holidays (charter) for UK residents. The large majority of these holidays are made by air to the popular destinations in the mainland and islands of Southern Europe and North Africa. The market was already concentrated with four large companies having some 80 per cent of the market in question. The rest of the market was fragmented amongst a large number of smaller players, none of them fully integrated and most with market shares of 1 per cent or less. The takeover would create a market structure in which the remaining three big companies would collectively have a dominant position, as First Choice would disappear both as a competitor and as a supplier of charter airline seats to the non-integrated operators. The short-haul package tour constitutes a market different from the one of long-haul package tour. Due to differences in price, consumer preferences (such as length of journey, flight time, "jet-lag", prerogative thoughts about typical charter destinations), etc, the two types of destinations are not substitutable. Both parties operate their own (charter) airlines and some of the seats are also supplied to third parties (other operators). Tour operators use almost exclusively charter flights since scheduled airlines are more expensive and may result in flight changes, which is inconvenient for the customers. Accordingly scheduled flights are not a viable substitute for charter flights. Although flying prices have increased in recent years and the entry of low cost airlines (Ryanair, Virgin Express) they do not constitute a sufficient constraint to charter flights and they do not always operate to popular tourist resorts. This was the first time the Commission prohibited a merger on grounds of collective dominance between more than two companies.

6.3.1 Collective dominance in the package tour market

The merger would not lead to the creation or reinforcement of a dominant position by a single firm, but to a situation of collective dominance. Airtours argued at the hearing that collective dominance could be thought of as a cartel, but without explicit cartel agreement, cartel meetings etc. It also explained that such tacit cartel would be unstable in the UK market because there was no retaliatory mechanism, which would prevent any of the participants in the tacit cartel from "cheating". As set out by the

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[83] Sunk costs relates to expenses at the entry of a new market (advertising, etc), which will be lost in

Commission in previous cases and confirmed by the CFI most recently in Gencor/Lonrho, active collusive conduct of any kind is not a prerequisite for collective dominance to occur. It is sufficient that adaptation to market conditions causes an anti-competitive market outcome. As the Commission's decision in the Gencor/Loner case stated, a collective dominant position "can occur where a mere adaptation by members of the oligopoly to market conditions causes anti-competitive parallel behaviour whereby the oligopoly becomes dominant."[84] Active collusion is therefore not required where the members of the oligopoly are able to behave to an appreciable extent independently of their remaining competitors as well as the customers and consumers. In the Airtours decision the Commission went further by stating that it is not a necessary condition of collective dominance for the oligopolists to always behave as if there were one or more explicit agreements (e.g. to fix prices or capacity or share the market). "It is sufficient that the merger makes it rational for the oligopolists, in adapting themselves to market conditions, to act – individually – in ways which will substantially reduce competition between them and as a result of which they may act independently of their entourage."[85] In its statement of objections, the Commission identified certain features of market structure and operations, which had been identified as making anti-competitive outcomes, in particular, collective dominance more likely. The Commission stated that there does not even have to be a mechanism of retaliation, where, as in Airtours, there are strong incentives to reduce competition coercion may be unnecessary. In this case, the Commission has come to the conclusion that the substantial concentration in the market structure, the resulting increase in its already considerable transparency and the weakened ability of the smaller tours operators and of potential entrants to compete will make it rational for the three major players to avoid or reduce competition by constraining the overall capacity.

6.3.2 Market structure

The Commission's own assessment of market shares for the short-haul package holidays gives approximately 32 per cent for the parties combined (Airtours 21 per cent, First Choice 11 per cent), 27 per cent for Thomson and 20 per cent for Thomas Cook. The market structure was, prior to the merger, characterised by four large

case of an exit of the market.

[84] See supra note 43, at para 140.

[85] See supra note 20, at para 54.

operators, each integrated both upstream into charter airline operation and downstream into travel agency, plus a numerous "fringe" of small, largely non-integrated independent tour operators and agents. In the Commission's view, the overall effect of these factors is that, even in absence of the notified merger, the tour operating market is one in which the smaller suppliers are not able to offer effective competition to the four large ones. Consequently, the market outcome is effectively decided by the competition between the four large integrated suppliers.

A number of characteristic, which make the market conducive to oligopolistic dominance, will be discussed below in the context of the package tour market, for example, product homogeneity, low demand growth, low price sensitivity of demand, similar cost structures of the main suppliers, high market transparency, extensive commercial links between the major suppliers, substantial entry barriers and insignificant buyer power. The merger would, according to the Commission, reinforce all these characteristics with exception of the first two, and contribute to the creation of a situation of collective dominance among the three large operators that would remain after the merger.

6.3.3 Product homogeneity

There are two aspects of this case that differs from the Commission's earlier reasoning in collective dominance cases. Previous cases have focused on collusion on prices and have concerned more homogenous products. However, the Commission found a homogenous nature of short-haul package tours due to the fact that short-haul package tours are to a large extent a standardised product and the large majority of the offer consists of three star/intermediate hotels. This was confirmed by market studies, which showed that about 85 per cent of the customers was influenced mainly by price in their choice of holiday, whereas brand loyalty is of little importance.[86] This case had a product that were much more heterogeneous than in previous cases. Accordingly, it would make it less likely to reach collusive prices. However, the concern of oligopolistic dominance related to the prices are of minor importance in this case. The concern regards rather the pre-fixed capacity. Capacity is basically fixed 12-18 months in advance of the season. For this reason, considerable price discounts with respect to the catalogue prices are expected when the departure dates

[86] See supra note 20, at para 88.

are approaching. Consequently, they will be unable to change their supply during the season and in this industry there is, therefore, no need to co-ordinate on price. The crucial question is how much capacity is put onto the market and the collusive outcome is likely to occur, not on price but on capacity. This sort of collusion is unlikely to be found many other sectors since capacity decisions constrain the firms for a long time and therefore make punishment very painful for the companies.

6.3.4 Low Demand Growth

The Commission found that market growth is not likely to provide a stimulus to competition within the foreseeable future. Furthermore, the “fringe” was at a competitive disadvantage compared to the integrated operators. Any market growth was, therefore, likely to be captured by the three operators. However, this did not increase the concern of oligopolistic dominance. On the contrary, volatility of demand made the market more conducive to oligopolistic dominance. Volatility in demand in combination with the fact that it is easier to increase than to decrease capacity means that it was rational for the major operators to adopt a conservative approach to capacity decisions. In particular, the volatility of demand made it rational to limit planned capacity and then add capacity later, if demands prove to be stronger than expected. Capacity limitations risked occurring even though the demand in this market was previewed to remain stable.

6.3.5 Low Price Sensitivity

This factor was connected to the price elasticity in the market. Price was an important parameter in the market in question. Due to the barriers to growth facing the small independent operators, this implied that the integrated operators could increase the overall level of prices, if they were to behave in a parallel way. This would not necessary have to imply an increase in the catalogue prices but due to the fact that a tighter market would be created, this could lead to a reduction in the number of holidays sold in the “last minute”, which would lead to a higher average price. [87]

6.3.6 Conclusion on Airtours

The Commission here applied the concept of collective dominance to an industry whose features are considerably different from those, which have characterised the

[87] See supra note 20, at para 98.

industries involved in previous cases of collective dominance. In this market there are absence of total product homogeneity and a high variability of market shares over time. Furthermore, this is the first case concerning collective dominance where the anticipated collusion would take place on reduction of capacities. The Commission has argued that the collusive outcome is likely to occur not on price, but on capacity during the planning season.[88] Previously the risk of collusion on price had created the major concern for the Commission. In this case, the impact of the vertical integration of the parties is particularly interesting and this seems to play an important role in the competition analysis. The outcome of the pending judgment of the CFI will provide interesting guidance of the scope of collective dominance.

7. Comparison with collective dominance under Article 82

7.1 Article 82 EC

Legal textual concerns never occurred to the same extent regarding oligopolistic dominance under Article 82, since the provision expressly authorises the Commission to intervene against "one or more undertakings" abusing a dominant position. The concept was first applied in Italian Flat Glass and later confirmed in, inter alia, Almelo[89] and DIP[90]. In Compagnie Maritime Belge, the applicant stated that collective dominance should only apply to undertakings, each detaining a dominant position, which would imply that collective dominance did not embrace the undertakings position in the market structure and the conditions of competition in general, but only the behaviour of the undertakings in question. However, the CFI established that Article 86 (now 82) could be applied to situations where several companies together hold a dominant position. Furthermore, the applicant in Compagnie Maritime Belge held that abuse of collective dominance only could appear if <u>all</u> of the undertakings holding a collective dominant position acted in breach of Article 82. In that case, a refusal of delivery by a single undertaking, holding together with other undertakings a joint dominant position, could not constitute a breach of Article 82. The Commission did not agree on this point. Collective dominance occurs when one or more undertakings abuse their positions even though not all the companies in collective dominance behave in the same way.

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[88] See supra note 20, at para 91.
[89] C-393/92 Almelo v. Energiebedrijf Ijsselmig

According to the case law of Article 82, the presence of links was during a long time still to be added. The Court ruled in both Italian Flat Glass and Almelo that links are a necessary criterion in order to establish abuse of collective dominant position. For a long time there was uncertainty concerning the scope and purpose of links in merger cases. The judgment from the Court in Gencor contributed with an awaited clarification on this point. Links are no longer a necessary criterion in order to establish collective dominance in merger cases. Whether this ruling also applied to Article 82 was uncertain until the judgment Compagnie Maritime Belge. In principle, there would seem to be no legal obstacle to this.[91] In March 2000 the ECJ ruled on this matter after an appeal by the parties of the judgment from the CFI. The Court held that a dominant position may be held by two or more economic entities legally independent of each other and within the scope of the provisions of Article 81, provided that from an economic point of view they present themselves or act together in a particular market as a collective entity. Whether undertakings constitute a collective entity is established by examining the economic links which give rise to a connection between the undertakings concerned. Such links may be the result of the terms of implementation of an agreement between them, but "…the existence of an agreement or of other links in law is not indispensable to a finding of a collective dominant position; such a finding may be based on other connecting factors and would depend on an economic assessment and, in particular, on an assessment of the structure of the market in question."[92]

A question that occurs by this statement is whether the description of collective dominance here above reconciles the case-law under Article 82 and the case-law on oligopolistic dominance in merger cases. How far this statement may be interpreted will be interesting to see. What can be concluded from this judgment is that the case-law under Article 82 has changed from having been more behavioural orientated in the early case-law. It now seems like the Court has adopted a more structural point of view. The focus on the structure of the market is an essential feature when assessing mergers. A question remains whether links under Article 82 can be interpreted as far as in Gencor v. Commission*,* where the CFI ruled that the market structure could rise

[90] Case C-142/94 DIP and others v. Commission
[91] Antonio F. Bavasso, Gencor: A Judicial Review of the Commission's Policy and Practice, World Competition 22 (4): 45-65, 1999, Kluwer Law International

to an economic factor.[93] It is clear that a market structure in itself may be enough to block a merger. This seems not to be excluded from a literal reading of Compagnie Maritime Belge. However, such a broad interpretation of paragraph 45 here above in addition with an oligopolistic market structure (similarity in cost, transparency and few players) would seem too ambitious to establish collective dominance under Article 82. A major difference between the two situations remains. In cartel cases, not only dominance but also abuse has to be established. The market structure may amount to a link, but can never amount to abuse per se. The case-law under Article 82 has been referred to in merger cases.[94] A question is whether the ruling in Gencor can be used as a reference in a cartel case, where the CFI established that the market structure could rise to an economic factor. The concept of collective dominance may be the same for the two provisions, but there must be a distinction in the application of the concept. This distinction is fundamental for the legal certainty for the companies acting on an oligopolistic market.

Another question is whether the Commission is supposed to use Article 81 and 82 to deal with market structures at all. The application of Article 81 and 82 risks being too unpredictable, if the behavioural orientated approach is abandoned. The Commission has gained an efficient tool in applying the concept of collective dominance in order to prevent the creation or the reinforcement of too concentrated markets. However, it would create a considerable legal unpredictability if the Commission had the power to punish firms in oligopolistic markets only because their behaviour not always is beneficial for the competition. Only in clear cases of abuse, the Commission should use their power and intervene. In a market structure where tacit collusion is likely to take place, the Commission shall refrain from intervening if the players only adapt themselves intelligently on the market. Only when the parties abuse the collusive behaviour and the situation of collusion, tacit or explicit, is evident, the Commission's intervening is motivated. Therefore, in merger investigations a correct assessment of the post-merger markets is of greatest importance, since once a harmful market structure is established the intervention of the Commission and the national competition authorities will be limited to tackle alleged anti-competitive behaviour of the firms.

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[92] See supra note 30, at para 45.
[93] see supra note 11, para 276 and 6.2.10.1

7.2 Concerted practice

The interpretation of Article 81 and the notion of concerted practice are far-reaching. The principle of concerted practice was established ICI[95] and has thereafter been repeated in a number of cases, for example Suiker Unie. The Court ruled that: "…each economic operator must determine independently the policy which he intends to adopt on the common market. Although this requirement of independence does not deprive the undertakings the right to adapt themselves intelligently to the existing and anticipated conduct of their competitors, it does, however, strictly preclude any direct or indirect contact between such operators the object or the effect whereof is either to influence the conduct on the market of an actual or potential competitor or to disclose to such a competitor the course of conduct which they themselves have decided to adopt (…) on the market". [96]

The difficulty is to distinguish concerted practice from parallel conduct such as simultaneity of price announcements as a result of the very high degree of transparency of the market, which could be explained by the nature and the structure of the market. This decision requires a deep economic assessment of several aspects as the special features of an oligopolistic market with few competitors, high entry barrier, a reduced degree of competition, etc.

7.2.1 Parallel behaviour

The Commission considers itself empowered to prohibit concentrations on the sole basis of a creation or a reinforcement of a market structure, which is likely to facilitate the adoption of a common position by the parties resulting from conscious parallel behaviour. The parallelism does not even have to be conscious but may arise from unilateral effects or co-ordinated effects of the merger. Unilateral effects appear from the mere fact that the number of competitors in the market will be reduced. The parties will have less incentive to compete. Without any co-ordinate actions, the unilateral effects will lead to price increases, regardless of any collusion. This is often a consequence when the two largest companies merge, which may result in harmful effects on a sound competition. The concept of unilateral and co-ordinated effects

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[94] See for example the Gencor judgment refers to Italian Flat Glass when discussing the relevance of links in para 276.
[95] Case 48/69 ICI v. Commission, para 119

comes from American competition law, but has been discussed more and more in Europe since the Commission started to apply a more economic approach to the assessment of mergers. From the practitioners' point of view, clarifications of the concept of unilateral effects and co-ordinated effects have been requested.

The principles of concerted practice and parallel behaviour are of greatest importance when examining market structures in cases of alleged collective dominance. Merger control aims at preventing situations where the firms can adopt themselves intelligently on the market, while in cases of alleged concerted practice the task of the Commission is to distinguish non-collusive intelligent behaviour from illegal contacts between the firms.

8. Conclusion

8.1 The conceptual framework for horizontal merger appraisal

The purpose of merger control is to prevent mergers that imply reduced economic welfare. It is equally desirable that the merger control approves of mergers, which are likely to enhance welfare. Welfare may be improved by mergers, which lead to lower costs and prices. Welfare is normally harmed by mergers, which result in higher prices and do not reduce costs. Mergers which entail higher prices through reduced competition but lead to lower costs because of improved efficiency are, in theory, ambiguous in their effect on welfare, although in practice a merger which raised prices is likely to be seen with suspicion.

8.2 The impact of the merger on the competitors

When prices rise through either unilateral or co-ordinated effects, competitors of the merged firms will benefit from this. If the merged firms have made a unilateral output reduction or price increase, competitors will benefit by finding that the merged firm's price rise has raised demand for their own output, permitting them to raise the prices of their products. If the merger has co-ordinated effects, competitors will clearly benefit through the enhanced ability to agree on tacitly or explicitly collusive arrangements. However, competitors will have legitimate grounds for complaining

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[96] Case 40/73 Suiker Unie v. Commission, para 173-174

about a merger that increases the merged firm's ability to engage in exclusionary practices, which might force the rival company out of the market. This kind of practices often flows from vertical mergers. An example of such merger was the prohibited take over of First Choice by Airtours.

8.3 Guidelines are required

The European merger control provides no guidelines concerning the market shares of the merging companies. In the preamble of the Merger Regulation, a lower limit of 25 per cent has been established to cases of single dominance in order for the Commission to initiate an examination. As it was stated in the Commission's decision Alcatel/AEG Kabel, where the combined market share was estimated to 25 per cent and the market share of the closest competitor amounted to 23 per cent: "…EC merger control does not contain a legal presumption of the existence of a collective dominant oligopoly as soon as certain companies have a combined market share. Where three companies have a combined market share exceeding 50 per cent there is a legal presumption under German law (…) Under the Regulation such a presumption which amounts to a reversal of the burden of proof does not exist." On the contrary, the Commission would have to demonstrate in all cases that effective competition could not be expected on structural grounds between the leading companies in a highly concentrated market. The Commission did not find that the concentration would lead to collective dominance and the merger was cleared without conditions. However, this shows an extended application of the doctrine of collective dominance. In the U.S. practice there are fixed thresholds, which indicates a presumption of oligopolistic dominance. The EC practice attempts to go around similar limitations by calculating the combined market shares not only of the merging companies but also the market shares of the most important competitors. This follows from the fact that, in the EC practice there are two criteria that have to be fulfilled in order to prohibit a merger; (i) create or reinforce a dominant position and (ii) significantly impede the common market. In US practice only the last criterion has to be established. One question that may be asked is why the EC competition policy keeps the former criterion. What we can conclude after having examined the Commission's practice is that it seems to be an on-going congruence between the EC and U.S. practice, since the Commission circumvent the rules by adding market shares in order to find a sufficient degree of market power. Guidelines of the main principles would be of great use.

8.4 Inconsistency in the Commission's practice

In order to establish the market power of the post-merger situation, there are several factors to consider. The Mannesmann/Vallourec/Ilva[97] case serves as example for the Commission's large "marge de manoeuvre" to develop basic principles and to adopt these principles. In this case, especially the explanations of the Commission regarding potential competition are contrary to the principles developed by the Commission in Aérospatiale-Alénia/De Havilland[98] and Nestlé/Perrier. Depending on the willingness to consider future potential competition from outside Europe as a reasonable factor in the market assessment has resulted in different conclusions.[99] The risk of inconsistency in the Commission's practice must be eliminated. The judgments Kali & Salz and Gencor, which emphasise the importance of a thorough economic analysis carried out by the Commission, the development of case-law principles and the expected guidelines, will hopefully prevent and reduce the risk on inconsequence on the concept of collective dominance.

9. Analysis section

9.1 Efficiency considerations

A distinction shall be made between the case where the merger give raise to concerns of unilateral price increase and the case where the merger makes it more likely that firms increase prices through coordinated behaviour. The latter corresponds to the concept of collective dominance, whereas the former does not correspond to correspond to the concept of single dominance. In a case where only a few companies will be left after a merger, but none of them will have enough market power to be dominant and collusion will not be likely, hence there is no collective dominance, the merger can however still be detrimental. In that case the EC policy of merger control is unable to prohibit the merger, since the Regulation requires the creation or the reinforcement of a dominant position. This is a disadvantage of the EC Merger control compared to the US Merger policy, where the focus is more on efficiency

[97] See supra note 69.
[98] Case No IV/M.053 Aeorspatiale-Alénia/de Havilland
[99] Hildebrand, supra note at pp 410 ff

gains and detrimental effect of the post-merger market than on the finding of a dominant position, whether single or collective. Therefore, there exists a large gap in the EC merger control since all mergers, which allow firms to unilaterally raise prices but do not create or reinforce a dominant position, cannot be prohibited. The opposite distortion when focusing on dominance is that mergers, which are welfare enhancing, might be prohibited since they give rise to a dominant position. As long as dominance in the meaning of Article 2 of the Merger Regulation has to be established, the concept of collective dominance is the only way to block harmful mergers, whose market shares are too insignificant to give rise to single dominance.

What may be missing in the Merger Regulation is the explicit taking into account of efficiency gains, which result in both producer and consumer surplus. It is not clear that the Merger Regulation excludes the considerations of efficiency gains. The wording does not exclude efficiency gains, even if it is not explicitly allowed. Although Article 1.1 (b) of the Merger Regulation states that the Commission shall take into account, among other things "…the interest of the intermediate and ultimate consumers and the development of technical and economic progress provided that it is to consumer's advantage and does not form an obstacle to competition." However, the legislative history of the Merger Regulation has sometimes been mentioned as supporting the view that there exists no efficiency defence in the EC competition law. In a previous draft of the Regulation, a sentence from the final text that would have allowed for some efficiency defence was suppressed from the final text, allegedly showing explicit intention of the legislators not to allow for such defence. This view has support from some authors that interpret the regulation in the light of the preparatory work, which shows that social, political and industrial arguments shall always be of subsidiary importance when assessing a merger. However, perhaps this only means that the intention was to avoid the possibility that this argument would be used to support industrial policy arguments and not in order to exclude efficiency arguments in general. It seems to be a contradiction between the spirit of the legislators and the use of an efficiency defence.[100]

The extension of the concept of collective dominance makes it possible for the Commission to cover a distortion in the Merger Regulation, which does not allow

[100] ECLR [2000] 199-207, M. Motta, "EC Merger Policy and the Airtours case"

prohibiting welfare detrimental mergers unless they reinforce or create a single dominant position. This forces the Commission to use the concept of collective dominance also in cases where it is very difficult to prove that the merger will increase collusion on the market. By consequence this creates a risk of lack of transparency and unpredictability with very uncertain outcomes in the courts. However, it would in these cases be relatively easy to prove the merger would create detrimental welfare effects. Indeed, the Merger Regulation establishes that " a concentration which creates or reinforces a dominant position….". Therefore, the finding of a dominant position is a necessary condition for prohibiting a merger. There exists therefore a gap in the EC Merger Control since certain mergers, which allow firms to unilaterally raise prices without creating or reinforcing a dominant position, cannot be prohibited. The possibility of prohibiting mergers which give rise to unilateral effects of market power even when there is no dominance should be introduced explicitly in the Merger Regulation, even if this probably would require a modification in the Regulation 4064/89.

Another distortion in the EC merger policy is the risk of using the concept of collective dominance to mergers that might be welfare enhancing. This distortion comes from the lack of efficiency gain considerations. This can occur, for example, when two firms intend to merge and this merger will entail so large efficiency gains that the consumers would benefit from lower post-merger prices. This merger would benefit the consumers but according to the EC competition rules it would have been prohibited because of the failure to consider efficiency effects and due the fact that it would have created a dominant position. However, it is not clear that, even in an extreme case of a merger, it that would result in both producer surplus and consumer surplus, the consumers will be able to take advantage from the cost-savings. When cost reductions have been claimed by the parties, for example in Aerospatiale-Alénia/DeHavilland, the Commission has dismissed those claims on various grounds. According to the Merger Regulation, nothing excludes the consideration of efficiency gains, even if one cannot say by reading the wording of the provision that this is explicitly allowed. Neither the preamble, nor the preparatory work supports the existence of an efficiency defence. On the contrary, social political and industrial policy arguments may always be of second importance and not be used in the assessment of mergers. Anyway, so far the Commission has not ruled out the using of an efficiency defence by the parties, even if very little attention has been paid to this aspect, at least explicitly. However, if the Commission were takes this aspect into account implicitly, it would be better if it started to make an explicit use of the efficiency defence for transparency reasons.[101]

To conclude, there are two aspects to be considered in merger assessment on grounds of collective dominance. On one hand, by focusing on the criterion of dominance, it will result in some welfare detrimental mergers to be approved. On the other hand, the absence of efficiency considerations may block beneficial mergers. Moreover, the lack of an explicit statement of efficiency considerations risk to negatively affect the transparency in the decision making process.

[101] ECLR [1999] p. 26-27, P.D. Camesasca, "The Explicit Efficiency Defense in Merger Control: Does it Make the Difference?"

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