COMPARISON WITH THE EU NON-HORIZONTAL AND UK MERGER ASSESSMENT GUIDELINES

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On January 10, 2020, the U.S. Department of Justice and the Federal Trade Commission (US agencies) published their long-awaited Draft Vertical Merger Guidelines (US-DVMG). In this paper, we compare and contrast the content of the US-DVMG to the analogous EU non-horizontal merger guidelines (EU-NHMG)[1] and UK Merger Assessment Guidelines (UK-MAG).[2] The relationship between guidelines in major jurisdictions guides some of our thinking about the strengths and weaknesses of the draft guidelines as they stand, which we present in a separate and concurrent submission titled "Comments on the January 2020 Draft Vertical Merger Guidelines."

The US-DVMG document is undeniably short, at just nine pages. As a result, there are inevitably some limitations to its scope (the number of topics that it explicitly addresses) and its depth of coverage (the detail with which it does so) relative to the equivalent guidelines in other jurisdictions. There are also

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[1] "Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings", Official Journal of the European Union, 2008/C 265/07, https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52008XC1018(03)&qid=1579197948739&from=EN.

[2] UK Merger Assessment Guidelines, *Competition Commission and Office of Fair Trading*, September 2010, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/284449/OFT1254.pdf. The UK-MAG was subsequently adopted by the board of the UK's Competition and Markets Authority (CMA) when these former UK competition agencies merged in 2014.

notable substantive differences compared with the EU-NHMG and UK-MAG in relation to specific topics.

We begin by comparing the scope and depth of guidance (Section 1) and then compare and contrast them in greater detail in terms of the following:

- **Market definition and related products**: (Section 2) The US-DVMG makes clear that the US agencies will ordinarily define at least one relevant market (and may define several), but it suggests that in analyzing any given vertical theory of harm they will not define markets both upstream and downstream. Instead, the US agencies develop the concept of a "related product" to a relevant market.[3] In practice the EU and UK authorities define markets both upstream and downstream, even though the UK-MAG cautions that market definition does not determine the outcome of the analysis of competitive effects in any mechanistic way.[4]

- **Safe harbor threshold:** (Section 3) The US-DVMG introduces a different safe harbor threshold compared to the EU-NHMG and UK-MAG. The proposed US safe harbor may prove to be more or less strict than those in the EU and UK, but in at least one significant aspect it is markedly more strict (the market share element of the test is set at 20% in US-DVMG, lower than the 30% threshold in the EU-NHMG). It therefore may result in a wider set of mergers receiving attention beyond an evaluation of whether the safe harbor threshold is satisfied.

- **Unilateral effects**: (Section 4) Unlike the EU and UK guidelines, the section in the US-DVMG on Unilateral Effects related to Foreclosure and Raising Rivals' Costs does not adopt the language of input- and/or customer foreclosure, although the discussion is recognisably consistent with the basic approach laid out in the EU-NHMG and UK-MAG. Instead, the US-DVMG adopts the terminology of a "related product" to a relevant market, thereby attempting to cover both input foreclosure and customer foreclosure at the same time. Potentially this could allow other, yet unspecified, theories of harm to be considered under the US-DVMG in the future.

[3] US-DVMG, p. 2.

[4] UK-MAG, ¶ 5.2.2.

- **Coordinated effects**: (Section 5) The coverage of coordinated effects of vertical mergers in the US-DVMG largely mirrors that in the EU-NHMG but does so at a considerably higher level of abstraction, without the same texture. In particular, there is much less by way of description of scenarios or factors that may be relevant for a specific set of facts. The US-DVMG does not attempt to draw lessons from the economic literature as to the specific industry characteristics (e.g., post-merger industry symmetry) that may be associated with an increased risk of coordination resulting from the merger.

- **Efficiencies – except double Marginalization**: (Section 6) The EU-NHMG considers double marginalization as a potential efficiency expressly rather than affording it a special status as the US-DVMG appears to do. The result is that while there is considerable commonality, there are also potentially important differences in approach. For example, the EU-NHMG requires parties to consider whether an argued double marginalization efficiency is merger-specific whereas the test in the US-DVMG emphasizes evaluating the pre-merger situation. Put crudely, this may for example prove to be the difference between evaluating whether it would be possible to use vertical contracts absent the merger to avoid double marginalization (in the EU) and whether the parties actually did (in the US).

Even as the US-DVMG represents a noteworthy step toward convergence of enforcement relative to the fragments of guidance they will replace, these differences make clear that there is still a gap in approaches. Coordinating the advice and analysis of transactions across jurisdictions will likely remain a necessary challenge for some time to come.

1. Overall approach to guidance

The US-DVMG describes that "Vertical mergers combine firms or assets that operate at different stages of the same supply chain."[5] The EU-NHMG similarly

[5] US-DVMG, footnote 2, p. 1. See also the related but slightly different wording later in the document "Vertical mergers bring together assets used at different levels in the supply chain to make a final product." US-DVMG, p. 9.

describe vertical mergers as involving "companies operating at different levels of the supply chain. For example, when a manufacturer of a certain product (the 'upstream firm') merges with one of its distributors (the 'downstream firm'), this is called a vertical merger."[6]

The EU-NHMG and UK-MAG discuss each topic in more detail than the much more streamlined US-DVMG. They also offer guidance on a broader scope of mergers than the US-DVMG.

1.1. Scope of guidance

The EU-NHMG covers both conglomerate and vertical mergers. In contrast, the UK-MAG is a single document across all types of horizontal and non-horizontal mergers.[7] It also draws a distinction between vertical and diagonal mergers (i.e., those between "an upstream supplier and a downstream competitor of the customers that purchase the supplier's goods"[8]). In contrast, the US-DVMG covers vertical mergers, but does not distinguish diagonal mergers (although they may be covered within the definition of vertical mergers) and does not appear to cover conglomerate mergers (since its definition of vertical mergers refers to different stages of the supply chain).

A consequence is that connections between the US agencies' approach to analyzing vertical, conglomerate and diagonal mergers are not expressly drawn out in the US-DVMG.[9] This may be significant since there sometimes can be considerable debate in cases about whether the merger is best characterized as a vertical, horizontal or diagonal case. For example, European Commission

[6] EU-NHMG, ¶ 4.

[7] While there are potential advantages to a document with a narrow scope, there are also good reasons that the EU and UK sought to take an integrated approach. Since a decrease in mark-ups downstream may lead to higher demand upstream, one way to think about vertical mergers is that they will often bring complementary activities or products into a single firm. Moreover, as the EU guidelines describe, the distinction between different types of mergers (horizontal, conglomerate, and vertical) can sometimes be subtle. For example, "products may be supplied by some companies with the inputs already integrated (vertical relationship), whereas other producers leave it to the customers to select and assemble the inputs themselves (conglomerate relationship)." EU-NHMG, footnote 5, ¶ 5.

[8] UK-MAG, ¶ 5.6.2.

[9] The intent in the US-DVMG may be for the term "vertical merger" to cover diagonal mergers. The US-DVMG describes "Vertical mergers combine firms or assets that operate at different stages of the same supply chain." See US-DVMG, footnote 2, p. 1.

economists explicitly described that they faced such challenges in *Google/DoubleClick* soon after the EU-NHMG was released.[10]

To take another example, is the acquisition of a physician group by a hospital chain a vertical merger or, alternatively, a merger of complements? Ultimately the facts should drive the economic analysis, not the label. Moreover, as the UK-MAG describes: "Any given merger can have aspects of more than one of [vertical, conglomerate and diagonal effects]. For example, a merger may be characterized as part vertical and part diagonal in terms of its effects on competition."[11] By seeming to distinguish vertical mergers from other arrangements which can have the closely related economic effects (e.g., mergers between complementary products and services), the US-DVMG may risk inviting debate of form over substance.

1.2. Depth of guidance

The EU-NHMG and UK-MAG have a clearer consideration of input and customer foreclosure (since they are covered separately) and, throughout, offer a richer description of the factors they will consider in particular variations of the theory (e.g., which factors suggest an ability and which suggest an incentive to suppress competition, how do capacity constraints at one level affect the analysis, what types of contracts suggest a pre-existing ability to influence competition in the other market, is the possibility of sponsoring entry in one of the products a mitigating factor or a consequence of the effects of the conduct, and so forth). In this specific sense the EU-NHMG and UK-MAG provide more guidance to practitioners, while the US-DVMG is more abstract in character. There are of course potential advantages of the more abstract treatment including the virtue of avoiding distinctions without a difference. The flexibility in the US-DVMG may prove more resilient to the evolution of case law and the understanding of economic theory over time. The balance between providing specificity and retaining flexibility in a guidance document is firmly resolved on the side of retaining flexibility in the US-DVMG.

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[10] Papandropoulos, P. (2009) "Non-horizontal mergers: recent EC cases," *European Commission, DG Competition, Chief Economist Team*, p. 21, https://ec.europa.eu/dgs/competition/economist/non_horizontal_mergers.pdf.

[11] UK-MAG, ¶ 5.6.3.

2. Market definition

The US-DVMG makes clear that the "Agencies will normally identify one or more relevant markets in which the merger may substantially lessen competition."[12] There are a number of questions that nonetheless arise. First, should the US agencies always define at least the two relevant markets and, if not, what is the alternative to doing so? Second, how should self-supply or "captive" sales be treated in market definition? We discuss each in turn.

2.1. Will the US agencies define both markets?

The US-DVMG does not expressly describe either that the US agencies will always define both upstream and downstream markets or that they will not. There may be an implication that the US agencies will not define a market for the related product.

Neither the EU nor the UK guidelines explicitly describe that their approach to vertical cases always involves defining both upstream and downstream markets in vertical cases. Indeed, there is no substantive discussion of market definition in the EU-NHMG.[13] However, in practice, the EU and UK authorities do define both upstream and downstream markets. In addition, the application of the EU's safe harbor rule does implicitly suggest that it will always define at least the "markets concerned" since it must do so to calculate the required market shares: "The Commission is unlikely to find concern in non-horizontal mergers ... where the market share post-merger of the new entity *in each of the markets concerned* is below 30% and the post-merger HHI is below 2,000."[14] To illustrate, in the recent significant vertical case *Tesco/Booker* wherein one of the UK's major supermarket chains (Tesco) acquired a wholesaler (Booker),[15] the CMA examined three levels of the supply chain: grocery retailing, grocery

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[12] US-DVMG, p. 2

[13] Indeed, the only occurrence of the words "market definition" in EU-NHMG is in a footnote noting that "The calculation of market shares depends critically on market definition" and providing a reference to separate guidelines on market definition (EU-MD). See EU-NHMG, footnote 2, ¶ 24. Market definition is instead considered in "Commission Notice on the definition of relevant market for the purposes of Community competition law" (97/C 372/03), https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:31997Y1209(01)&from=EN. (EU-MDEF).

[14] EU-NHMG, ¶ 25, emphasis added.

[15] "Tesco and Booker: A report on the anticipated acquisition by Tesco PLC of Booker Group plc," Competition & Markets Authority, December 20th, 2017, https://assets.publishing.service.gov.uk/media/5a3a7dd7ed915d618542b8df/tesco-booker-final-report.pdf.

wholesaling and grocery supply. For each, it concluded on the appropriate product market and the appropriate geographic market.

That said, the UK-MAG considers market definition for both horizontal and vertical mergers primarily as (only) a framework for the analysis of the competitive effects of the merger,[16] stating that the "boundaries of the market do not determine the outcome of the Authorities' analysis of the competitive effects of the merger in any mechanistic way."[17]

Avoiding defining the boundaries of a second market will sometimes have advantages for the US agencies. In particular, it is well known that it can be challenging to define markets in the presence of market power because of the cellophane fallacy.[18] In conduct cases, the cellophane fallacy can be avoided by approaching the problem in reverse by asking, for example, whether prices would be significantly lower but for the conduct at issue in the case (i.e., would price go down significantly without the market power the conduct is assumed to convey). This kind of "price-down" test may reduce to establishing a market definition by proving effects. This approach makes market definition less relevant than it has historically been in merger analysis.

Most vertical merger theories presume the kind of market power that may make this exercise challenging. For example, when following a partial input foreclosure strategy, the merged firm would raise the price charged upstream to independent suppliers and, in so doing, raise its rivals' costs downstream. Asking whether the upstream firm has an incentive to raise the price, however, depends on whether the merged firm can benefit from the resulting market power downstream. Similarly, the merged entity may only benefit from market power downstream if the merged entity does raise upstream prices to their downstream division's competitors. Thus, a reason the US-DVMG may leave open the possibility of reducing the number of markets being defined could be to avoid the need to find a way through the seemingly circular questions.

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[16] The words 'frame of reference' do not appear in the 2010 UK-MAG but have been adopted by the CMA subsequently in cases to capture this idea.

[17] UK-MAG, ¶ 5.2.2.

[18] Philip Nelson, "Monopoly Power, Market Definition, and the Cellophane Fallacy," Economists Incorporated, The United States Department of Justice, June 25th, 2015, https://www.justice.gov/atr/monopoly-power-market-definition-and-cellophane-fallacy.

2.2. The related market alternative to market definition

The US-DVMG introduces the concept of a “related product,” describing that a related product or service is one that (a) is supplied by the merged firm; (b) is vertically related to the products and services in the relevant market; and (c) to which access by the merged firm’s rivals affects competition in the relevant market.[19] The US-DVMG goes on to describe that “A related product could be, for example, an input, a means of distribution, or access to a set of customers.”[20] Note that the last of these – “access to a set of customers” – is an unusual-sounding product. We presume this could be something like a media service offering content providers carriage and, therefore, access to the customers already subscribed to the service. But, we note that this example makes it particularly clear that inferring the chain of product flow and the limitations of strictly vertical transactions can become a linguistic challenge.

One potential motivation for introducing the concept of a “related product” may be to emphasize that one product is often the input that contributes to the joint production of the downstream product. For example, in the case of an upstream manufacturer selling to a downstream retailer, the latter provides retail services which, combined with the manufacturer’s product, constitute the downstream product. That is, in this simple example the downstream product is a bundle of the manufacturer’s product and the (retailer’s) service. In such a customer foreclosure case, access to the retailer’s service is made unavailable to competing manufacturers.

In any event, the intended application of the “relevant product” concept may become clearer if Example 1 in the US-DVMG is clarified. Example 1 describes a merger between a retailer and manufacturer of cleaning products, and states that the US agencies “may identify two relevant markets.”[21] In particular, putting geographic markets to one side, the example states that the US agencies may identify:

1. A first potential relevant product market (downstream) as the “supply of cleaning products to retail customers.”[22] For this relevant product market, the “related product [upstream] is the supply of the cleaning products by the

[19] US-DVMG, p. 2.
[20] US-DVMG, p. 2.
[21] US-DVMG, p. 2.
[22] US-DVMG, p. 2.

manufacturer to retailers."[23] That is, in this case the related product would be the input from the manufacturer to the retailer that is necessary to be a retailer of that manufacturer's cleaning products. This first part of the example seems to apply to input foreclosure cases.

2. A second potential relevant product market (upstream) as the "supply of cleaning products to retailers."[24] For this relevant product market, "the related product is the purchase [upstream] or distribution of that manufacturer's cleaning products to sell to retail customers [downstream]."[25] That is, in this case the related product is either the upstream product (an input necessary to being a retailer) or the downstream services (the other input required to be a retailer). This second part of the example seems to apply to customer foreclosure cases.

If the purpose of Example 1 is to illustrate that the US agencies will apply their guidelines symmetrically, we believe it would be clearer if the language used in this section of the US-DVMG distinguished in the final version of the guidelines between the upstream and downstream parts of this industry.

A complementary potential motivation for introducing the concept of the "related product" may be a desire by the US agencies for the guidelines to avoid expressly drawing out the distinction between input foreclosure and customer foreclosure. Instead, the US-DVMG provides examples which bring out that both input foreclosure and customer foreclosure can be considered through the lens of the "related product." This approach is distinctly different from that in the EU and UK guidelines, where explicit distinctions are drawn. Indeed, much of the structure of the EU guidelines is geared around this distinction.[26]

The consequence is that the US guidelines are thinner in detail and there is less economic terminology. The latter will be helpful for non-specialist judges. However, there is also undoubtedly a downside from this light-touch approach in terms of a reduction in clarity; by avoiding terms such as "input foreclosure" and "customer foreclosure", the guidelines are effectively adopting a framework with an additional level of abstraction – one which must simultaneously describe the framework for analysis for both theories of harm (and indeed any others that the US agencies may have in mind). As we have previously

[23] US-DVMG, p. 2.

[24] US-DVMG, p. 2.

[25] US-DVMG, p. 2.

[26] EU-NHMG, ¶¶ 31-77.

described, the US-DVMG does not provide the same level of clarity about the analysis that the US agencies intend to undertake to evaluate a given theory of harm as is provided in the EU-NHMG and UK-MAG.

The US agencies may be comfortable with some ambiguity around the need for market definition since they note that at least some economic tools, particularly merger simulation, do not in any event rely on market definition. We discuss the US-DVMG's observations in relation to merger simulation further in "Use of Economic Models" below.

2.3. How should self-supply (captive sales) be treated?

The relegation of market definition to the US-HMG means that the US-DVMG is silent on vertical merger-specific elements of market definition, in particular whether internal supply or, to use the language of the US 1984 Merger Guidelines, "Captive production and consumption of the relevant product by vertically integrated firms are part of the overall market supply and demand."[27] The EU-NHMG similarly relegates market definition to the EU-MDEF while noting that "Special care must be taken in contexts where vertically integrated companies supply products internally."[28]

In contrast, in respect to self-supply, the UK-MAG describes that there are special considerations when some firms buy their inputs in a merchant market, and this makes it necessary to consider whether (a) production of the input used for self-supply by the merging parties, and (b) self-supply by potential customers of the merged firms, should be included in the relevant market for assessing competitive effects on input markets.[29] In relation to (a) the UK-MAG describes:

> "The Authorities will generally follow the principle that captive production by the firms will be included in the relevant market only if it can be demonstrated that it would be profitable for the supplier to forgo its use and sell into the merchant market in response to a SSNIP."[30]

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[27] 1984 Merger Guidelines, https://www.justice.gov/archives/atr/1984-merger-guidelines.
[28] EU-NHMG, footnote 2, ¶ 24.
[29] UK-MAG, ¶ 5.2.20.
[30] UK-MAG, ¶ 5.2.20.

And in relation to (b), the UK-MAG describes:

> "The Authorities will also consider whether self-supply by potential customers of the merger firms should be included in the relevant market. The Authorities will generally include self-supply if the ability of customers to choose this option affects the profitability of a price rise by the hypothetical monopolist."[31]

3. Share thresholds

An important line in the US-DVMG outlines a proposed two-pronged test for a merger to benefit from what may or may not be a safe harbor. Namely, the US agencies are unlikely to challenge a vertical merger where (a) the parties to the merger "have a share in the relevant market of less than 20 percent" and (b) "the related product is used in less than 20 percent of the relevant market."[32] This test appears to be cumulative so that both elements of the test must be satisfied in order for the proposed merger to benefit from the safe harbor rule.[33]

The EU-NHMG describes instead that:

> "The Commission is unlikely to find concern in non-horizontal mergers, be it of a coordinated or of a non-coordinated nature, where the market share post-merger of the new entity in each of the markets concerned is below 30 % and the post-merger HHI is below 2000."[34]

As a result, the US and EU guidelines[35] will allow different sets of mergers to benefit from the safe harbor. Significantly, the draft US guidelines may allow a narrower set of mergers to benefit from the safe harbor than under the EU and UK regimes in terms of market shares. There is then a contrast between the US-DVMG which requires use of the related product in less than 20 per cent of the

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[31] UK-MAG, ¶ 5.2.20.

[32] US-DVMG, p. 3.

[33] We note that the guidelines (a) do not define what "used in" means and that there may be multiple possible measures of "use" in practical settings, and (b) do not clearly link the notion of "use" of the related product to a particular economic concept relevant for one or more vertical theories of harm. In cases where either element of the safe harbor test fails, the vertical theory of harm itself in a given case must be assessed. See section 5 below.

[34] EU-NHMG, ¶ 25. A footnote is omitted from the quotation, but our discussion turns to it next.

[35] The UK follows the approach in the EU guidelines on this point.

relevant market and the EU and UK regimes which only extend the safe harbor to mergers in at most moderately concentrated markets. A post-merger HHI of 2000 would, after all, imply a post-merger market less concentrated than the position with five equal-sized firms each with 20% market shares.

To the extent that vertical agreements and vertical mergers are substitutes, it makes sense for there to be alignment between ex-post enforcement safe harbors and ex-ante merger control safe harbors in order to avoid there being a particular advantage to structuring a deal as a merger rather than a vertical agreement or vice versa. The EU-NHMG follows the European Commission's vertical agreements regulation when adopting a 30 per cent market share safe harbor for vertical agreements without certain types of severe restrictions.[36] The EU-NHMG describes that a finding of concern is unlikely while post-merger market shares "in each of the markets concerned" satisfy the threshold, and also that competition concerns may also be "less likely" if one market share is just above the threshold and the other is substantially below:

> "Where a merged entity would have a market share just above the 30 % threshold on one market but substantially below on other, related, markets competition concerns will be less likely."[37]

The harbor may be safe but, to continue the nautical analogy, the boats in the harbor are still subject to some risk of particularly stormy conditions. In particular, both the US-DVMG and EU-NHMG provide caveats allowing mergers that satisfy the safe harbor threshold to nonetheless give rise to competitive concerns in particular circumstances. The US-DVMG states that the share of the relevant market that uses the related product may understate the scope for material effects "if the related product is relatively new, and its share of use in the relevant market is rapidly growing."[38] The EU-NHMG similarly describes that it will not extensively investigate mergers that satisfy

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[36] "Commission Regulation (EU) No 330/2010 of April 20th, 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices," *Official Journal of the European Union*, April 23rd, 2010, L 102/2, https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32010R0330&from=EN. The 30 % share figure also appears in the previous version of the regulation "Commission Regulation (EC) No 2790/1999 of December 22nd, 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices", *Official Journal of the European Communities*, December 29th, 1999, L 336/21, https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:31999R2790&from=EN.

[37] EU-NHMG, footnote 3, ¶25.

[38] US-DVMG, p. 3.

the safe harbor threshold, except where "special circumstances" apply. These may include:

> "(a) a merger involves a company that is likely to expand significantly in the near future, e.g. because of a recent innovation;
>
> (b) there are significant cross-shareholdings or cross-directorships among the market participants;
>
> (c) one of the merging firms is a firm with a high likelihood of disrupting coordinated conduct;
>
> (d) indications of past or ongoing coordination, or facilitating practices, are present."[39]

In addition, the EU-NHMG also makes clear that "Non-horizontal mergers pose no threat to effective competition unless the merged entity has a significant degree of market power (which does not necessarily amount to dominance) in at least one of the markets concerned."[40]

The UK-MAG simply describes that the CMA will "not often" investigate mergers which satisfy the safe harbor thresholds without providing additional information.[41] It is unclear whether the authors of the US-DVMG and the UK-MAG have considered the relevance of the wider set of examples provided by the EU-NHMG and have decided that they are either unnecessary or that they disagree with them.

4. Evidence and unilateral effects

The US-DVMG covers in two sub-sections respectively:

a) Foreclosure and Raising Rivals' Costs
b) Access to Competitively Sensitive Information

[39] EU-NHMG, ¶ 26.
[40] EU-NHMG, ¶ 23.
[41] UK-MAG, ¶ 5.3.5.

Largely the discussion of Foreclosure and Raising Rivals' Costs appears consistent with the framework laid out explicitly and considerably more expansively in the EU-NHMG. In particular, it describes that:

> "A vertical merger may diminish competition by allowing the merged firm to profitably weaken or remove the competitive constraint from one or more of its actual or potential rivals in the relevant market by changing the terms of those rivals' access to one or more related products. For example, the merged firm may be able to raise its rivals' costs by charging a higher price for the related products or by lowering service or product quality. The merged firm could also refuse to supply rivals with the related products altogether ('foreclosure')."[42]

The discussion of Access to Competitively Sensitive Information is the one area in the US-DVMG where the discussion is arguably slightly more extensive than in the EU-NHMG, albeit the comparison involves a distinction between the length of a single paragraph in each case.

In this section, we discuss each topic in turn.

4.1. Foreclosure and raising rivals' costs

The US-DVMG describes that the US agencies may consider whether:

> "(1) The merged firm's foreclosure of, or raising costs of, one or more rivals would cause those rivals to lose sales (for example, if they are forced out of the market, if they are deterred from innovating, entering or expanding, or cannot finance these activities, or if they have incentives to pass on higher costs through higher prices), or to otherwise compete less aggressively for customers' business;
>
> (2) The merged firm's business in the relevant market would benefit (for example if some portion of those lost sales would be diverted to the merged firm);

[42] US-DVMG, p. 4.

(3) Capturing this benefit through merger may make foreclosure, or raising rivals' costs, profitable even though it would not have been profitable prior to the merger; and,

(4) The magnitude of likely foreclosure or raising rivals' costs is not de minimis such that it would substantially lessen competition."[43]

This basic structure appears to largely mirror the approach taken in the EU-NHMG, but without using the terms "Ability to foreclose" (condition 1), "Incentive to foreclose" (conditions 2 and 3) and "Overall likely impact on effective competition" (condition 4). In particular, the terms in quotations are the sub-section headings in the EU-NHMG in both the sub-section on input foreclosure (IV.A.1) and the sub-section on customer foreclosure (IV.A.2). Similarly, this approach mirrors closely the one laid out in paragraph 5.6.6 of the UK guidelines.

4.1.1. De minimis effects?

The most significant difference may be the use of the *de minimis* test for effects in the US-DVMG. The language in the US-DVMG appears to categorize the magnitude of any effect which is not *de minimis* as being substantial. But, as Commissioner Wilson asked, what is the magnitude of anticompetitive effect that should be viewed as *de minimis* "in light of EDM [Elimination of Double Marginalization] and likely vertical efficiencies?"[44]

The question of just how substantial a concern needs to be to warrant an investigation or challenge is familiar ground across all three jurisdictions. The range of possibilities is encapsulated in a longstanding decision of the UK House of Lords:

"... no recourse need be made to dictionaries to establish that 'substantial' accommodates a wide range of meanings. At one extreme there is not trifling, at the other there is nearly complete, as where someone says he is in substantial agreement with what has just been

[43] US-DVMG, p. 5.

[44] "Concurring Statement of Christine S. Wilson," *Publication of FTC-DOJ Draft Vertical Merger Guidelines for Public Comment*, File No. P810034, January 10th, 2020, https://www.ftc.gov/system/files/documents/public_statements/1561709/p810034wilsonvmgconcur.pdf.

> said. In between there exists many shades of meaning drawing colour for their context, but the meaning of the word has been reflected in the decided cases ...."[45]

In these terms, the *de minimis* criteria in the US-DVMG appears akin to the "extreme" interpretation of substantial as meaning "not trifling."

The EU-NHMG emphasizes instead that the EU's Significant Impediment to Effective Competition (SIEC) test will only be satisfied in a customer foreclosure case if "a sufficiently large fraction of upstream output is affected by the revenue decreases resulting from the vertical merger."[46] In particular, the EU-NHMG notes that "If there remain a number of upstream competitors that are not affected, competition from those firms may be sufficient to prevent prices from rising in the upstream market and, consequently, in the downstream market."[47] Thus, while "sufficiently large" may seem like just another way to say "substantial" and so take the debate no further forwards, the approach does at least begin to describe factors which may be relevant to the Commission's assessment of the likely magnitude of effects.

The UK agencies have been similarly careful to avoid getting drawn into attempts to define the difference between a lessening of competition and a "substantial" lessening of competition (SLC) and have, in consequence, avoided introducing an explicit numerical materiality threshold even for horizontal mergers, whether a certain percentage price increase or level of harm. Nonetheless, the UK-MAG states that "while there can be no fixed definition [of the term substantial], the area or areas considered must be of such size, character and importance as to make it worth consideration for the purposes of merger control."[48] This suggests a threshold at least as big, and probably bigger, than *de minimis*. Moreover, the UK-MAG describes that an SLC arising from foreclosure will only be possible where the merging parties have the ability and incentive to foreclose. In respect of effects:

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45 R v. MMC ex parte, South Yorkshire Transport [1993] 1 W.L.R.23, p. 29. Cited in transcript (day 2, p. 2, line 1) for the hearing of Unichem Limited v. Office of Fair Trading in the Competition Appeals Tribunal, https://www.catribunal.org.uk/sites/default/files/Tran1049Unichem180205.pdf.

46 EU-NHMG, ¶ 74.

47 EU-NHMG, ¶ 74.

48 UK-MAG, ¶ 3.3.6.

1. In the case of input foreclosure the UK-MAG describes: “To the extent that the merged firm has both the ability and incentive to increase prices so as to foreclose *to some extent* its rival manufacturers, the Authorities will consider the impact of such foreclosure on competition in the downstream market.”[49]
2. In the case of customer foreclosure the UK-MAG imposes: “the impact of such customer foreclosure on the upstream market would be significant in terms of rivalry, taking due account of any efficiencies that enhanced the merged firm’s own incentives to compete.”[50]

4.1.2. Use of economic models

To evaluate the four criteria,[51] the US-DVMG suggests that, where sufficient data is available, the US agencies may construct merger simulation models designed to quantify the likely unilateral price effects resulting from the merger. They not only reference the term “merger simulations,” but also note that such models “often include independent price responses by non-merging firms.”[52] While the “often” allows for exceptions, this guidance suggests a preference for these methods over techniques such as Vertical Gross Upward Pricing Pressure Index (vGUPPI), which do not allow for price responses by non-merging firms. This language precisely mirrors language contained in the US-HMG.[53] However, unlike the US-DVMG, the US-HMG also includes language both describing in some detail and endorsing upward pricing pressure analysis.[54] Presumably the US agencies will consider vGUPPI models where sufficient data to construct a merger simulation model are not available.

Merger simulations have been considered in EU merger practice since *Tom-Tom/TeleAtlas*.[55,56] The CMA applied vGUPPI in its 2017 *Tesco/Booker* merger

[49] UK-MAG, ¶ 5.6.12, emphasis added.

[50] UK-MAG, ¶ 5.6.13.

[51] US-DVMG, p. 5.

[52] US-DVMG, p. 4.

[53] US-HMG, p. 21.

[54] “The Agencies rely much more on the value of diverted sales than on the level of the HHI for diagnosing unilateral price effects in markets with differentiated products,” US-HMG, p. 21.

[55] See Davis and Garces (2009), *Quantitative Techniques for Competition and Antitrust Analysis*, Princeton University Press, chapter 10.

[56] We note also that the discussion of merger simulation contains an observation which probably goes beyond vertical mergers, namely the Agencies describe that “Agencies do **not** treat merger simulation evidence as conclusive in itself, and place more weight on whether their merger simulations

inquiry. In doing so, the CMA considered whether the results of its analysis were robust to vGUPPI's implicit assumptions.[57]

In the UK-MAG, the CMA describes an analysis that follows the logic of unilateral pricing pressure tests.[58] In respect of vertical mergers, the UK-MAG considers in some detail how it may evaluate a partial input foreclosure theory of harm[59] and provides more compact remarks in relation to total foreclosure and customer foreclosure.[60] The text in the UK-MAG does not explicitly mention either vertical merger simulation or vGUPPI, but it does focus on the topic of whether the merger would change the parties' incentives to increase their prices to rival manufacturers post-merger.[61]

In practice, all the agencies seem likely to continue applying a pragmatic approach to the particular economic tools used in their merger evaluation. Their decisions will be driven at least in part by the availability of the required information.

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consistently predict substantial price increases than on the precise prediction of any single simulation" (US-DVMG, p. 4, emphasis added).

[57] "Tesco and Booker: A report on the anticipated acquisition by Tesco PLC of Booker Group plc," *Competition & Markets Authority*, December 20th, 2017, https://assets.publishing.service.gov.uk/media/5a3a7dd7ed915d618542b8df/tesco-booker-final-report.pdf.

In particular, see "Appendix C: Vertical effects incentives analysis." The CMA considered two "key" implicit assumptions made by the Parties when submitting their vGUPPI analysis: (a) The assumption that the merged entity could adjust aspects of its offer at the level of individual stores costlessly. If, instead, parameter flexing were costly – for example because it would involve increases in prices at non-overlapping stores, or of reputational damage from targeted flexing – the CMA argued this would tend to reduce the unilateral incentive to increase prices. (Appendix C, ¶¶ 22-24) (b) The assumption that it was reasonable to proxy the wholesale demand elasticity (the losses that would directly result from Booker increasing its wholesale prices before accounting for any subsequent recapture resulting from overlaps with Tesco) with the inverse of Booker's wholesale margin. The CMA considered this is a "reasonable assumption in theory" (Appendix C, ¶ 27) while noting that the assumption is "subject to the caveat that variable margins are themselves difficult to measure and that with non-linear pricing the relationship between margins and elasticity is less straightforward." (Appendix C, ¶ 29)

[58] UK-MAG, ¶¶ 5.4.7-5.4.11.

[59] UK-MAG, ¶¶ 5.6.9-5.6.11.

[60] UK-MAG, ¶ 5.6.13.

[61] UK-MAG, ¶ 5.6.11.

4.1.3. The examples

The section in the US-DVMG on Foreclosure and Raising Rivals' Costs lays out a number of examples. Using the terminology from the EU-NHMG and perhaps more familiar to practitioners:

- Example 3 describes what is sometimes called "vertical arithmetic" for a theory of harm that there would be total input foreclosure, that is, the merged firm may entirely stop supplying an input to competitors downstream.
- Example 4 describes a partial input foreclosure wherein the merged firm continues to offer to supply downstream competitors from its upstream division, but increases the price it charges to independent downstream competitors post-merger.
- Example 5 describes total input foreclosure of a potential new entrant into a relevant downstream market.
- Example 6 describes a form of partial customer foreclosure wherein the distributor division of the merged firm finds it profitable to raise the price of wholesale distribution after the merger even if the price rise were not profitable pre-merger.

These examples are clearly helpful additions to the US-DVMG. However, the guidelines do not describe – at least in the context of the examples – the implicit assumptions. In practice, the economic analysis of vertical mergers can involve developing an understanding of:

- The nature of vertical contracts that could be used in each of the factual and the counterfactual scenarios. The US-DVMG describes very generally, in the context of the section on Evidence of Adverse Competitive Effects, that "[p]re-existing contractual relationships may affect a range of relevant market characteristics."[62]
    - » In terms of the factual, the EU-NHMG describes for example that "the presence of exclusive contracts between the merged entity and independent input providers may limit the ability of downstream rivals to have adequate access to inputs."[63] It goes on to state that "the nature of the supply contracts between upstream suppliers and the downstream independent firms may be

[62] US-DVMG, p. 4.
[63] EU-NHMG, ¶ 36.

important in this respect. For instance, when these contracts use a price system combining a fixed fee and a per-unit supply price, the effect on downstream competitors' marginal costs may be affected less than when these contracts involve only per-unit supply prices."[64]

   - In terms of the counterfactual, the EU-NHMG describes that "[t]he efficiencies associated with the elimination of double mark-ups may … not always be merger specific because vertical cooperation or vertical agreements may, short of a merger, achieve similar benefits with less anti-competitive effects."[65] The US-DVMG makes a similar point, although only in relation to the elimination of double marginalization.[66] We describe the implications of using different types of vertical contracts on the analysis of foreclosure in more detail in Section 6 below.

- Whether the incentive to engage in a foreclosure strategy is greater than the incentive to engage in other, procompetitive and yet more profitable, strategies that the merging parties could pursue. The US-DVMG and EU-NHMG focus on whether foreclosure is a feasible and profitable strategy, without placing particular emphasis on whether foreclosure would be the most profitable strategy available to the merging parties. Similarly, the UK-MAG formulates the "incentive" question explicitly as whether the merged firm would "find it profitable" to foreclose.[67] That said, the EU-NHMG does describe that "the Commission examines both the incentives to adopt such conduct and the factors liable to reduce, or even eliminate, those incentives."[68] We also note that the EU-NHMG describes that "the Commission may take into account … the content of internal strategic documents such as business plans."[69] Although the language only suggests such plans "may" be taken into account, it is clearly the case that internal strategic documents will turn out to be helpful to the parties in some cases and unhelpful in others.
- The potential counterstrategies available. For example, citing *Boeing/Hughes*[70] the EU-NHMG describes that in the context of

[64] EU-NHMG, footnote 2, ¶ 38.
[65] EU-NHMG, footnote 7, ¶ 55.
[66] US-DVMG, p. 7.
[67] UK-MAG, ¶ 5.6.6.
[68] EU-NHMG, ¶ 46.
[69] EU-NHMG, ¶ 45.
[70] CaseCOMP/M.1879 — Boeing/Hughes (2000).

customer foreclosure considerations it will consider "whether there are effective and timely counter-strategies, sustainable over time, that the rival firms would be likely to deploy."[71] There is no explicit discussion of counterstrategies to foreclosure in the US-DVMG.

- The potential consequences of engaging in unlawful conduct. The EU-NHMR also discusses its approach to unlawful conduct: "Conduct may be unlawful *inter alia* because of competition rules or sector-specific rules at the EU or national levels. This appraisal, however, does not require an exhaustive and detailed examination of the rules of the various legal orders which might be applicable and of the enforcement policy practiced within them. Moreover, the illegality of a conduct may be likely to provide significant disincentives for the merged entity to engage in such conduct only in certain circumstances. In particular, the Commission will consider, on the basis of a summary analysis: (i) the likelihood that this conduct would be clearly, or highly probably, unlawful under Community law, (ii) the likelihood that this illegal conduct could be detected, and (iii) the penalties which could be imposed."[72]

To close our discussion of the examples in the US-DVMG, we note that the last line of Example 6, which appears to illustrate the mechanism at work in a customer foreclosure theory of harm, seems to introduce an asymmetry relative to input foreclosure cases by introducing a materiality threshold. In particular, the last sentence of the text in Example 6 describes the effects conditions that: "If the merged firm has a sufficiently important position … and the price rise it imposes … is sufficiently high … competition maybe substantially lessened."[73] Is this threshold meant to be different from the *de minimis* condition laid out in condition (4)? Or, is this just articulating what condition (4) might involve in a way that is supposed to be relevant for all of the examples?

4.2. Commercially sensitive information

In contrast to a number of other aspects, while still very brief, the US-DVMG actually has more text than the EU and UK guidelines in relation to the theory of harm that a vertical merger may result in the combined firm gaining access

[71] EU-NHMG, ¶ 67.
[72] EU-NHMG, ¶ 46.
[73] US-DVMG, p. 6.

to and control of sensitive business information. The thrust of the concern raised mirrors the EU and UK guidelines where they describe:

> "The merged entity may, by vertically integrating, gain access to commercially sensitive information regarding the upstream or downstream activities of rivals[74]. For instance, by becoming the supplier of a downstream competitor, a company may obtain critical information, which allows it to price less aggressively in the downstream market to the detriment of consumers."[75,76]

The EU and UK guidelines also describe that "[i]t may also put competitors at a competitive disadvantage, thereby dissuading them to enter or expand in the market."[77] The US-DVMG adds some additional color to this concern describing that: "Relatedly, rivals may refrain from doing business with the merged firm rather than risk that the merged firm would use their competitively sensitive business information as described above. They may become less effective competitors if they are forced to rely on less preferred trading partners, or if they pay higher prices because they have fewer competing options."[78]

5. Coordinated effects

The US-DVMG deals with coordinated effects analysis specific to vertical cases in less than a page, while referring the reader to the discussion in Section 7 of the US-HMG, highlighting in particular that the theories of harm discussed in both guidance documents "are not exhaustive, but rather are illustrations of the

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[74] See Case COMP/M.1879 — Boeing/Hughes (2000); Case COMP/M.2510 — Cendant/Galileo, point 37; Case COMP/M.2738 — Gees/Unison, point 21; Case COMP/M.2925 — Charterhouse/CDC/Telediffusion de France, point37-38;CaseCOMP/M.3440— EDP/ENL/GDP(2004).

[75] See, e.g., Case COMP/M.2822 — ENBW/ENI/GVS (2002), point 56; Case COMP/M.3440 — EDP/ENI/GDP (2004), points 368-379; CaseCOMP/M.3653—Siemens/VATech (2005), points 159-164.

[76] See EU-NHMG, ¶ 78; see also UK-MAG, ¶ 5.6.13 (last bullet).

[77] The UK-MAG includes references to the anticipated acquisition by Boots Group plc of Alliance UniChem plc, OFT, May 2006, as well as BSkyB/ITV, CC, December 2007, where such a theory of harm was raised but not relied upon, and subsequently dismissed. UK-MAG, footnote 73.

[78] US-DVMG, p. 7.

manner in which a merger may lessen competition due to coordinated effects."[79]

5.1. Eliminating mavericks

In terms of the specific comments in relation to vertical mergers, the US-DVMG initially focuses on the situation when a vertical merger "by eliminating or hobbling a maverick firm"[80] would, in the counterfactual, play an important role in preventing or limiting anticompetitive coordination in the relevant market. The situations are not distinguished, but elimination could potentially refer to either the acquisition of a maverick firm or its total foreclosure. Hobbling a maverick firm may refer to the results of a partial foreclosure strategy whereby its input costs are increased or distribution opportunities decreased following a vertical merger.

The EU-NHMG also describes in particular that:

> "A vertical merger may also involve the elimination of a disruptive buyer in a market. If upstream firms view sales to a particular buyer as sufficiently important, they may be tempted to deviate from the terms of co-ordination in an effort to secure their business. Similarly, a large buyer may be able to tempt the co-ordinating firms to deviate from these terms by concentrating a large amount of its requirements on one supplier or by offering long term contracts. The acquisition of such a buyer may increase the risk of co-ordination in a market."[81]

5.2. Changes to conditions for coordination

The US-DVMG highlights that coordinated effects can arise in other ways, including when the merger or merged firm's access to confidential information facilitates "(a) reaching a tacit agreement among market participants, (b) detecting cheating on such an agreement, or (c) punishing cheating firms."[82] These three conditions are closely related to those identified by Stigler (1964),[83] that tacit agreements or concerted practices require some form or agreement or

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[79] US-DVMG, p. 8.

[80] US-DVMG, p. 8.

[81] EU-NHMG, ¶ 90.

[82] US-DVMG, page 8.

[83] Stigler (1964), "A Theory of Oligopoly," *The Journal of Political Economy*, Volume 72, Issue 1, pp. 44-61.

understanding, an ability to monitor competitors, or sometimes markets to infer cheating and some mechanism for enforcement so as to discipline cheating.

In Europe, the Stigler conditions are closely related to the conditions for tacit coordination described in the *Airtours* decision and so known as the Airtours conditions.[84] Accordingly, the EU-NHMG describes its analysis of coordinated effects under the headings: Reaching terms of coordination (this phraseology avoids the use of Stigler's word, "agreement"), monitoring deviations, deterrent mechanisms, and reactions of outsiders.[85]

The UK-MAG in paragraphs 5.5.9-5.5.18 describe a similar framework under the headings of (a) ability to reach and monitor the terms of coordination, (b) internal sustainability, and (c) external sustainability.

The text in relation to coordinated effects in both the UK-MAG and EU-NHMG is markedly more expansive than that in the US-DVMG.

In terms of the substance, while there is a great deal in common in the general framework adopted, it is perhaps notable that the EU and UK guidelines place a greater, or at least an explicit, emphasis on the (a) incentives for cooperation, as well as (b) the ability to cooperate:

- UK-MAG: Under the heading internal stability, the guidelines describe that the incentive to coordinate must be present as well as the deterrence mechanism: (a) "Coordination will be sustainable only where the additional profit from coordination is sufficiently high," and continues (b) "and there is an effective mechanism to punish deviation. If coordination is not sufficiently profitable, or the punishment is not sufficiently swift and painful, a firm may prefer to deviate."[86]
- EU-NHMG: These guidelines similarly place more explicit emphasis on the incentives, for example: "For coordinated effects to arise, the profit that firms could make by competing aggressively in the short term ('deviating') has to be less than the expected reduction in revenues that

[84] See CaseT-342/99, Airtours v Commission [2002] ECRII-2585, ¶ 62, referred to in a footnote to ¶ 81, EU-NHMG.

[85] EU-NHMG, ¶¶ 82-90.

[86] UK-MAG, ¶ 5.5.15.

> this behaviour would entail in the longer term, as it would be expected to trigger an aggressive response by competitors ('a punishment')."[87]

In addition, we note that the US-DVMG does not attempt to draw lessons from the economic literature as to the role of specific industry characteristics (e.g., post-merger industry symmetry) that may be associated with an increased risk of coordination resulting from the merger.

6. Efficiencies – except elimination of double marginalization

The efficiencies section of the US-DVMG describes that vertical mergers combine complementary economic functions and eliminate contracting frictions, so they "have the potential to create cognizable efficiencies that benefit competition and consumers." In particular:

> "Vertical mergers bring together assets used at different levels in the supply chain to make a final product. A single firm able to coordinate how these assets are used may be able to streamline production, inventory management, or distribution, or create innovative products in ways that would have been hard to achieve though arm's length contracts." [88]

Beyond that observation, the US-DVMG is remarkably quiet on efficiencies. It is notable through its absence that, while there is "potential … for cognizable efficiencies," there is no statement in the US-DVMG akin to those in the EU and UK guidelines that merger control for non-horizontal mergers is generally less likely to lead to competitive effects than horizontal mergers. In particular:

- The EU-NHMG describes that "[n]on-horizontal mergers are generally less likely to significantly impede effective competition than horizontal mergers."[89]
- The UK-MAG describes that "[n]on-horizontal mergers do not involve a direct loss of competition between firms in the same market, and it is a well-established principle that most are benign and do not raise

[87] EU-NHMG, ¶ 80.
[88] US-DVMG, p. 9.
[89] EU-NHMG, ¶ 11.

competition concerns. Nevertheless, some can weaken competition and may result in an SLC [substantial lessening of competition]."[90]

As a matter of economic substance, the one issue related to the area of efficiencies that does benefit from more specific text – indeed its own section (US-DVMG section 6) – is the potential for a vertical merger to eliminate double marginalization. As the US-DVMG describes, "Elimination of double marginalization may … benefit both the merged firm and buyers of the downstream product or service."[91]

The reason that double marginalization is not discussed in the efficiencies section (US-DVMG section 8) is also made clear in the text of the US-DVMG where it describes "[t]he Agencies will not challenge a merger if the net effect of elimination of double marginalization means that the merger is unlikely to be anticompetitive in any relevant market."[92] The logic of the US-DVMG appears to be that the elimination of double marginalization should perhaps be included in the foreclosure discussion (US-DVMG section 5) or at least more explicitly linked to it – if that is indeed what the US agencies intend in practice.

The US agencies thus propose to consider double marginalization as part of the analysis of whether there is a problem rather than as a part of their efficiencies analysis. Even so, consistent with the general approach to efficiencies, the text describes that "[t]he agencies generally rely on the parties to identify and demonstrate whether and how the merger eliminates double marginalization."[93]

The section on the elimination of double marginalization does identify express limits to the application of the argument, stating (a) it does not apply if the downstream firm cannot use the input from the upstream firm (e.g., because of incompatible technology); and (b) it may not apply in full if the merging parties already engaged in vertical contracting that "aligned their incentives," noting in particular, for example, that may be the case if a manufacturer uses two-part tariffs rather than uniform pricing in its contracts with retailers. [94]

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[90] UK-MAG, ¶ 5.6.1.
[91] US-DVMG, p. 7.
[92] US-DVMG, p. 7.
[93] US-DVMG, p. 7.
[94] US-DVMG, p. 7.

In the EU-NHMG, the Commission similarly describes that it applies the principles set out in its horizontal guidelines[95] which involve the cumulative conditions that, for the Commission to take account of efficiency claims in its assessment of the merger, the efficiencies have to benefit consumers, be merger-specific and be verifiable. The EU-NHMG considers double marginalization as a potential efficiency expressly rather than affording it special status as the US-DVMG appears to do.[96]

The US-DVMG also describes a particular limitation to the eliminating double marginalization argument, stating:

> "The effects of the elimination of double marginalization in the downstream market may also be offset by a change in pricing incentives working in the opposite direction: if the merged firm raises its price in the downstream market, downstream rivals may increase their sales, which could increase their demand for inputs from the merged firm's upstream business. Capturing this benefit through merger may make the downstream price increase more profitable."[97]

The EU-NHMG also highlights potential limitations to the elimination of double marginalization argument, namely:

> "It is important to recognise, however, that the problem of double mark-ups is not always present or significant pre-merger, for instance because the merging parties had already concluded a supply agreement with a price mechanism providing for volume discounts eliminating the mark-up. The efficiencies associated with the elimination of double mark-ups may thus not always be merger specific because vertical

[95] See EU-NHMG, ¶ 53 citing Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertaking, Official Journal of the European Union, C 31, 5.2.2004 s.

[96] There are, in practice, certainly examples of the European Commission blurring this distinction however by considering the elimination of double marginalization within its analysis of competitive effects – even if formally under the rubric of efficiencies. For example, in Case COMP/M.4854 — TOMTOM/TELE ATLAS (2008) under the heading "Effects in the downstream market" the decision includes a subsection with the heading 'Efficiencies' (p. 52). And goes on to describe the balancing test undertaken: "In order to estimate the overall effect of the proposed transaction taking into account the elimination of double mark-ups, the Commission estimated pre- and post-merger equilibrium prices using a simple model with linear demand. The model indicates that the overall impact of the vertical integration of TomTom and Tele Atlas, taking into account the elimination of the double marginalization by the integrated company, is a small decline in the average PND prices." (¶ 243)

[97] US-DVMG, p. 7.

> cooperation or vertical agreements may, short of a merger, achieve similar benefits with less anti-competitive effects."[98]

Thus, the EU-NHMG makes the point that the nature of vertical contracting matters; however, it uses volume discounts rather than two-part tariffs to make the same economic point as the US-DVMG but then emphasizes that the test in respect of efficiencies that involve evaluating whether the efficiencies are merger-specific. In contrast, the US-DVMG appears to emphasize that it will consider the situation *"prior to the merger*."[99] This distinction should, however, not be overstated. The economic literature suggests that vertical mergers and vertical contracting can be imperfect substitutes.[100] Therefore, while evidence on the limitations of pre-merger contracts are not necessarily determinative in the EU and UK, they will be evaluated when looking at whether the elimination of double marginalization is a merger-specific efficiency of the form recognized in these jurisdictions.

The EU-NHMG also expressly highlights another potential example of a limitation to the elimination of the double marginalization argument, namely that "a merger may not fully eliminate the double mark-up when the supply of the input is limited by capacity constraints and there is an equally profitable alternative use for the input. In such circumstances, the internal use of the input entails an opportunity cost for the vertically integrated company: using more of the input internally to increase output downstream means selling less in the alternative market. As a result, the incentive to use the input internally and increase output downstream is less than when there is no opportunity cost."[101]

[98] EU-NHMG, footnote 7, ¶ 55.

[99] See US-DVMG, p. 7: "The effects of the elimination of double marginalization may be lower if, prior to the merger, the merging parties already engaged in contracting that aligned their incentives, for example by using a two-part tariff with a fixed fee and low unit prices that incorporate no, or a small, margin."

[100] Grossman and Hart (1986), "The Costs and Benefits of Ownership: A Theory of Vertical and Lateral Integration," *Journal of Political Economy* 94(4): 691-719.

[101] EU-NHMG, footnote 7, ¶ 55.

7. Conclusion

The publication of US-DVMG has potential to be a significant milestone on the sometimes elusive path towards international convergence, almost a decade after the publication of the EU-NHMG. The extent and nature of international convergence is a major focus for international cooperation through organizations such as the International Competition Network (ICN)[102] and OECD Competition Committee.[103] In replacing outdated fragments of guidelines with a description of current practice, however abbreviated, the US agencies have significantly advanced this policy objective.

The US-DVMG will be a useful document for practitioners, even if this first draft is rather abstract. While the level of abstraction may give the US agencies more room for manoeuvre in future cases, the level of abstraction does take away from the extent that the document provides guidance to practitioners advising their clients, or for generalist judges deciding on challenges. The EU and UK guidelines describe the factors they will consider in much richer detail (e.g., margins, capacity constraints, types of contracts and the possibility of sponsoring entry and so forth). In this sense they provide more guidance than the US-DVMG and may remain go-to documents.

[102] The ICNs mission includes formulating “proposals for procedural and substantive convergence” (see https://www.internationalcompetitionnetwork.org/).

[103] See http://www.oecd.org/competition/.