

# CK TELECOM JUDGEMENT

Setting the standards

## COMPETITION

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**On 13 July, the Court of Justice of the European Union (the “CJEU”) delivered its long-awaited *CK Telecoms* judgement.<sup>1</sup> The Judgement is seen as a blow to further consolidation talks in the telecom industry. In it, the CJEU provides clarification on the standard of proof applicable in merger control in the European Union (“EU”) and the existence of “standard efficiencies”.**

### **Balancing pro- and anti-competitive effects of mergers**

The Judgement identifies a number of flaws in the General Court’s first instance judgement annulling the Commission’s decision to prohibit the merger of Three and O2 in the United Kingdom. For this reason, the CJEU quashes the General Court’s judgement and refers the case back to this court.<sup>2</sup>

With respect to the first question, the Judgement puts to rest a debate on the standard of proof applicable to so-called “gap cases” in EU merger control – i.e. mergers that do not create a dominant company but result in a significant impediment to effective competition (e.g. by removing an important competitor in an already concentrated market). As the CJEU confirms, the standard of proof applicable in all EU Merger Control clearance or blocking decisions is the balance of probabilities. In other words, the Commission should block a merger where it is more likely than not that it results in an impediment to competition and allow it otherwise.<sup>3</sup> This means that the standard of proof that the Commission must apply when finding a significant impediment to effective competition is the same as it applies when finding that the merger results in the creation or strengthening of a dominant position. In the words of the Chief Economist at the Directorate General for Competition (“DG Comp”) at the time of the merger, this judgement means that “merger control is not (yet) dead”.<sup>4</sup>

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<sup>1</sup> Court of Justice of the European Union, Judgment of the Court (Grand Chamber) of 13 July 2023, *European Commission v CK Telecoms UK Investments Ltd*. ECLI:EU:C:2023:561 (hereafter, the “Judgement”). All quotes are from the official English version.

<sup>2</sup> Judgement, paragraph 88.

<sup>3</sup> Judgement, paragraph 88. The merging parties are also allowed to propose remedies which resolve the competition concerns identified. In that case, the Commission can still approve the merger subject to those remedies.

<sup>4</sup> Quoted from a tweet of 13 July 2023. Available at <https://twitter.com/TomValletti/status/1679413396964364288>.

The judgement confirms the important role of economic analysis in the assessment of mergers, noting that the Commission's prospective economic analysis "must be carried out with great care",<sup>5</sup> while also reaffirming "the margin of discretion with respect to economic analysis" from which the Commission benefits.<sup>6</sup>

### Quantifying the balance

An interesting aspect of the Judgement related to the Commission's fourth appeal, concerning the interpretation of the Commission's quantitative analysis of likely price effects of the merger and its interpretation. In its decision, the Commission performed a calibrated merger simulation and used so-called 'price rise tests' to quantify the likely price effects of the merger.<sup>7</sup>

Qualitative analyses of price effects are frequently used by competition authorities to provide an indication of the potential price effects of a merger, particularly one where firms compete in differentiated products. These tests use economic models and data from the merging parties (such as margins and diversion ratios) to give an estimate of the rise in price that results from a horizontal merger. The tests can provide a first approximation of the effects of the merger, but (depending on the level of sophistication) may not take into account dynamic effects (such as product repositioning of competitors, new entry or consumer reactions) or cost-saving efficiencies. For example, most of these tests will always indicate a price increase after any horizontal merger irrespective of the size of the parties involved.

For this reason, it has been suggested that it is necessary to apply a threshold on the predicted price increase from such a price rise test in order to conclude that competition concerns exist. For example, in a seminal paper by Joseph Farrell and Carl Shapiro, the two former Deputy Assistant Attorney Generals for Economics at the Antitrust Division of the United States Department of Justice Antitrust Division propose the Upwards Pricing Pressure test as a simple initial screening test for potentially anti-competitive mergers and that a "standard deduction" is applied to account for merger-specific efficiencies which are typically hard to predict.<sup>8</sup>

In the present case, the General Court contended that the Commission erred in applying the threshold for its price test for two reasons.

On one hand, the General Court considered that the price effect was not significant because it was lower than the price effect found on two previous Commission merger decisions in the telecoms sector, which it had cleared. The CJEU considered that the General Court erred in law in this respect because past Commission decisions do not constitute a legal precedent.<sup>9</sup>

On the other hand, the General Court suggested that the Commission failed to account for "standard efficiencies" when applying its price effect estimation. Such "standard efficiencies" would arguably be in line with the original Farrell and Shapiro paper introducing the UPP test. The CJEU, however, held that *"to acknowledge that all concentrations give rise to 'standard' efficiencies would amount to creating a presumption, and therefore a reversal of the burden of proof, in respect of a particular category of efficiencies, whereas as is apparent from paragraphs 238 and 239 of the present judgment, that burden is borne by the undertakings."*<sup>10</sup>

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<sup>5</sup> Judgement, paragraph 85.

<sup>6</sup> *Idem*, paragraph 84.

<sup>7</sup> Commission, *Case M.7612 - Hutchison 3G UK / Telefonica UK*, 11 May 2015. Available online at [https://ec.europa.eu/competition/mergers/cases/decisions/m7612\\_6555\\_3.pdf](https://ec.europa.eu/competition/mergers/cases/decisions/m7612_6555_3.pdf) (the "Contested Decision"), paragraph 1192.

<sup>8</sup> Joseph Farrell and Carl Shapiro (2010), "Antitrust Evaluation of Horizontal Mergers: An Economic Alternative to Market Definition, *The B.E. Journal of Theoretical Economics*: Vol. 10: Iss. 1 (Policies perspectives), Article9. Available at: <http://www.bepress.com/bejte/vol10/iss1/art9>.

<sup>9</sup> Judgement, paragraph 220.

<sup>10</sup> Judgement, paragraph 243.

### Efficiencies take centre stage

In the absence of “*standard efficiencies*” or a significance threshold, any price increase resulting from a quantitative model would be sufficient to identify competition concerns, unless efficiencies are demonstrated. This highlights the importance of demonstrating efficiencies in future horizontal merger cases particularly those involving firms competing in oligopolistic differentiated products markets.

Ultimately, the interpretation of price rise analysis and the level at which competition concerns are identified depends on a variety of factors including (i) the level of demonstrated efficiencies, (ii) the uncertainty attached to the price rise analysis (for example, because of dynamic considerations), and (iii) whether there is a threshold for price rises to be considered to result in a *significant* impediment of effective competition. Competition authorities across Europe have applied varied thresholds when assessing price rise tests. Notably, in its Sainsbury’s/Asda decision the CMA found a substantial lessening of competition<sup>11</sup> in all local markets where the gross upwards pricing pressure (which is typically seen as a ceiling for any indicative price rise) was above 2.75%.<sup>12</sup>

Given that the model uncertainty and the definition of significant price rises are outside of the merging parties’ control, it is essential going forward that merging parties provide robust evidence to support their view on efficiencies, and they should do this already in an early stage.

The CJEU argues that this division of burden of proof achieves the desired outcome of blocking anti-competitive mergers and allowing pro-competitive mergers.<sup>13</sup> While this could be true in theory (in particular, merging companies are likely best placed to assess the efficiencies their merger creates), in practice that will only hold if the standard of proof applied to the assessment of efficiencies is the same as that for assessing harm, that is the balance of probabilities. The conventional view is that the standard of proof applied to assessing efficiencies has been high by authorities. In fact, they are rarely recognised in the context of EU Merger Control reviews. Going forward, if efficiencies will become critical for many horizontal “gap mergers” this will require robust analysis from merging parties and recognition of (verified) efficiencies by authorities.

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<sup>11</sup> The equivalent of a significant impediment of effective competition.

<sup>12</sup> CMA, *Anticipated merger between J Sainsbury PLC and Asda Group Ltd: Final report*, 25 April 2019, paragraph 46. Available online at [https://assets.publishing.service.gov.uk/media/5cc1ec1340f0b64031cfa6f0/Final\\_reportSA.pdf](https://assets.publishing.service.gov.uk/media/5cc1ec1340f0b64031cfa6f0/Final_reportSA.pdf).

<sup>13</sup> Judgement, paragraph 244.