

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

Executive Summary of the Roundtable on Non-Price Effects of Mergers

**Annex to the Summary Record of the 129th Meeting of the Competition Committee held on
6-8 June 2018**

6 June 2018

This Executive Summary by the OECD Secretariat contains the key findings from the discussion held during the 129th Meeting of the Competition Committee on 6 June 2018.

More documents related to this discussion can be found at www.oecd.org/daf/competition/non-price-effects-of-mergers.htm

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Executive Summary

By the Secretariat*

The OECD Competition Committee held a Roundtable on the subject of the non-price effects of mergers in June 2018. Based on the background paper prepared by the Secretariat, written submissions from delegates, and the contributions by expert panellists and delegates to the discussion, the following key points emerged:

1. Non-price competition encompasses a wide range of product characteristics and business decisions that can be as determinative of consumer welfare as price. However, in merger reviews, they play a central role in only a minority of decisions.

When a merger review involves the analysis of price effects, non-price effects tend to play a secondary role even when they may be relevant in assessing the competitive effects of the merger. Often, this is because price is considered a good proxy for any other effects: a merger that will result in price increases due to a lessening of competition is generally assumed to also harm innovation or quality. However, the ambiguity of empirical research on some non-price effects, and the more limited quantitative tools to analyse these effects, may also limit the extent to which agencies assess non-price competition.

2. Mergers can affect the incentive and ability of the merging firms to engage in innovation. The overall impact of a merger on innovation will depend on the specific circumstances of the market and merging firms. As a result, a case-by-case analysis will be needed.

There is a substantial body of economic literature investigating the relationship between competition and innovation, as well as the impact of mergers on innovation. Some papers emphasise the fact that mergers may reduce the incentive of merging firms to engage in innovation, since they will face less pressure to introduce new products and may in fact cannibalise their existing products. On the other hand, a merger could also combine the complementary innovation capacities of firms and increase their ability to develop new products. The mixed findings of the literature suggest that an automatic presumption that mergers are uniformly beneficial or harmful for innovation may not be warranted.

Competition authorities generally apply a case-by-case approach to assessing the impact of a merger on innovation. The specific analytical approach varies. In some past cases, the analysis of innovation has involved a narrow focus, for example identifying specific product development pipelines and assessing overlaps between firms. However, increasingly, authorities are facing the challenge of considering innovation more broadly. This could involve identifying the set of firms with sufficient innovation capacity to exert competitive pressure, regardless of whether those firms are currently product market or innovation competitors. Such an approach is a recognition of the importance of dynamic competition, and depending on the market could involve grappling with substantial

* This executive summary does not necessarily represent the consensus view of the Competition Committee. It does, however, identify key points from the discussion at the roundtable on non-price effects of mergers, including the views of a panel of experts, the delegates' oral and written contributions, and the background note prepared by the OECD Secretariat.

uncertainty. Business community stakeholders have called for greater clarity in guidelines when mergers are assessed using this approach.

3. Quality refers to a broad set of characteristics that differentiate one product from another. Anticompetitive mergers can lead to a degradation of quality but, like innovation, the academic literature suggests that a case-by-case analysis is needed.

The term “quality” can be defined as the range of product characteristics, other than price, which affect the value of the product to consumers. These characteristics can include functionality, durability, reliability, convenience of purchasing locations, design or aesthetic appeal, performance and safety. A merger can lessen the incentives of the merging firms to invest in product quality if it alleviates competitive pressure on those firms. On the other hand, mergers may also improve capacity to offer a given level of quality, or they may allow the merging firms to better coordinate the positioning of differentiated products in a way that improves consumer welfare. Assessing which of these effects prevails, and ensuring that any quality improvements do not come at the expense of a price increase that reduces overall welfare, requires a case-by-case analysis.

4. Privacy, or more broadly data protection, has been considered a dimension of quality in a limited number of recent merger decisions. The growing importance of consumer data in the business model of digital firms could mean that data protection becomes a more widely-recognised dimension of quality in future merger decisions.

Some scepticism has arisen with regard to incorporating privacy in merger control based on the view that it risks injecting subjectivity and alternative policy objectives into competition analysis. However, in at least some markets, data protection is a current differentiator among firms, and thus it can be considered a dimension of quality in standard analytical frameworks. Further, a lack of current differentiation among firms in terms of data protection does not necessarily mean it is not a valued dimension of quality for consumers - it may in fact suggest that there is insufficient competition in the market. That being said, competition authorities have expressed caution about injecting views about the importance of data protection into a merger assessment, and instead root their analysis in actual consumer preferences. This involves several complications; specifically: determining trade-offs with other characteristics such as functionality, identifying limitations to consumer information, and taking into account consumer behavioural biases.

5. Identifying which non-price dimensions of competition, if any, are important in the relevant market can be a particular challenge in merger review.

Some clear indicators that non-price factors matter include the presence of price regulation, zero price products, high price elasticity of demand, or frequent changes in product offerings based on specific features. When these indicators are absent, a case-by-case assessment is important to determine the characteristics that are important to consumers, and which are factored into firms’ competitive decision-making. The mere fact that a characteristic is not a current marker of differentiation among firms does not automatically suggest that it is not relevant to merger review (e.g. in terms of the merger’s effect on potential future product features).

6. Considering both price and non-price effects together can also be challenging in merger review. These effects may occur over different time periods, requiring competition authorities to weigh both static and dynamic competition effects together. Further, determining the relative weight that should be given to quantitative as opposed to qualitative evidence can be difficult, since the analysis of non-price effects generally requires qualitative evidence.

Some analytical techniques, such as discounting for uncertainty, adjusting prices for other dimensions, or merger simulation may be applied. However, in most cases, qualitative evidence will play a particularly important role, especially with respect to consumer preferences and the rationale for the transaction. In cases where there are likely opposing price and non-price effects, consideration should be given as to whether both effects are consistent with a lessening of competition. For example, a transaction that harms competition could result in both quality and price being increased beyond the competitive level.

7. When non-price competition is important, it can be incorporated into several stages of a case analysis; namely market definition, the competitive assessment, and the development of remedies.

In markets for which non-price competition plays a significant role, a market definition that focuses exclusively on price may introduce bias into a merger assessment. However, formal approaches to build in non-price dimensions in market definition tools, such as the small but significant non-transitory decrease in quality (SSNDQ) test, are rare in practice, due potentially to data limitations, conceptual critiques, and the lack of a specific methodology to follow. A flexible approach to market definition may therefore be required.

Dynamic analysis may be particularly important when conducting a competitive assessment that includes non-price effects. This analysis can cover how firm incentives will change, and the degree to which potential competition will emerge to challenge a post-merger firm, in terms of innovation efforts, quality or variety positioning, and even privacy protection.

The remedies applied to date to rectify concerns about non-price competition include both behavioural and structural measures that have also been used to address price concerns. However, the identification of remedies that adequately address potential non-price harms may be particularly challenging. This is because a remedy focusing on one dimension of competition may have unintended effects on other dimensions. Further, it is not clear that a behavioural commitment could address several aspects of non-price competition, such as innovation incentives.

8. Merging parties often submit claims of non-price efficiencies to competition authorities. On the one hand, these efficiencies are viewed with scepticism when accompanied with price increases, and when they are subject to uncertainty given their long timeframe. On the other hand, empirical studies do support the notion that mergers can in some circumstances produce improvements in non-price characteristics.

Non-price efficiencies are generally difficult to quantify, may not materialise for several years, and may appear to authorities as subjective claims by the parties to obtain merger approval. Some competition authorities have indicated that claimed non-price efficiencies often do not meet the standards they set with respect to merger specificity, feasibility and consumer benefits. Others observed that post-merger quality efficiencies identified by merging parties do not always materialise.

However, empirical studies of the impact of mergers on both innovation and quality suggest that efficiencies may, in some circumstances, arise in transactions. Competition authorities therefore face the challenge of weighing concerns about static price increases with broad claims about long-term dynamic efficiencies. Evidence regarding past mergers in the sector, and the track record of the merging firms, may help. Further efforts to quantify efficiencies, including discounts for uncertainty, may also help address concerns regarding

subjectivity. This relates to the importance of clear authority guidelines and analytical frameworks for assessing non-price efficiencies, in order to improve certainty and ensure that merging parties provide competition authorities with the evidence they need.