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The Trend Towards Increasing Intervention in UK Merger Control and Cases that Buck the Trend


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1 Introduction

This chapter focuses on the trend towards greater intervention by the UK Competition and Markets Authority ("CMA") in its substantive assessment of mergers. This includes, in particular, the growing proportion of qualifying mergers where the CMA finds a realistic prospect of a substantial lessening of competition ("SLC") at Phase 1 and an SLC at Phase 2. Notwithstanding this upward trend, the CMA continues to clear some potentially problematic mergers at Phase 1, even where it receives customer complaints. This chapter also discusses two such mergers that were cleared unconditionally at Phase 1 following consideration at a Case Review Meeting ("CRM"), namely *Unite/Liberty* (2019) and *Inspired/Novomatic* (2019).[1]

Whilst this chapter focuses on substantive assessment, these trends arise against the background of the CMA's adoption of a more interventionist stance on procedural matters (where the CMA has imposed penalties for infringements, as noted below) and jurisdictional matters (including an extensive application of the share of supply test – particularly in the context of so-called "killer acquisitions"). Both of these trends are explored below.

Before proceeding further, it is important to appreciate that a key feature of UK merger control is that it is ostensibly voluntary in the narrow sense that there is no obligation to seek merger clearance prior to completion. What this means in practice is that merger control risk may be transferred to the purchaser post-completion in the UK.[2] Given the trends described in this chapter, *caveat emptor* might be a good two-word summary of UK merger control. (Obviously, sellers bear execution risk in the context of conditional mergers, particularly since a proposed merger may signal to the firms' customers and suppliers that the underlying shareholders are not committed to the business.)

In this regard, businesses contemplating completing mergers before securing clearance should be mindful that the CMA is also taking a more interventionist approach to initial enforcement orders, which prohibit integrating the parties' businesses and require them to be hold separate.[3] Unsurprisingly, these orders are intrusive and the merging parties have begun challenging the CMA's approach to derogation requests for carve outs. In particular, observers will be following with interest Facebook's appeal to the Competition Appeal Tribunal ("CAT") as regards the CMA's treatment of Facebook's derogation requests in connection with its acquisition of Giphy.[4]

In addition, the CMA has also shown an increasing willingness to fine companies for breaching the terms of these enforcement orders,[5] and also to impose fines where companies' responses to Section 109 information requests are incomplete or delayed.[6]

Finally, and turning to the jurisdictional context, intervention trends also need to be judged in the context as to whether there is legal certainty as to the scope of UK merger control, including its international reach. In this regard, it is perhaps appropriate to contrast UK and EC merger control, with the latter being a mandatory pre-completion filing regime.[7]

In brief, EC merger control applies to Concentrations with a Community Dimension, and thus one may have narrowly defined debates on matters such as which undertakings have control (as to which the key issue is whether they have "decisive influence") and whether their turnover globally, across the EU and in Member States meets the requisite thresholds for the Concentration to have a Community Dimension. In contrast, the UK's jurisdictional thresholds are widely viewed as more flexible (read "elastic") than those that apply under the EU Merger Regulation ("EUMR") across multiple dimensions. For example, under UK merger control:

- Mergers may include the acquisition of assets, even in specific circumstances non-trading assets, such as in *Eurotunnel/Sea France*. This case was subject to various appeals, but the CMA's remitted decision that the acquisition of the assets constituted a merger was upheld by the Supreme Court in 2015, reversing the judgment of the Court of Appeal.
- Mergers may include the acquisition of "material influence". For example, in *Amazon/Deliveroo* (2020) the CMA held that Amazon's 16 per cent stake, limited other rights, and board director would confer material influence. Similarly, the CMA investigated *E.ON/RWE* (2019) based on RWE having a material influence over E.ON with a 16.67 per cent shareholding, and notwithstanding a relationship agreement limiting RWE's rights. The CMA cited RWE's industry status and expertise and shareholding relative to others as sufficient grounds for influence. In neither case would these shareholdings have conferred decisive influence for EUMR purposes.
- Mergers may qualify for investigation on the basis of the creating or enhancing of a 25 per cent share of supply in the UK or a substantial part thereof, as well as a turnover based test. This "share of supply test" enables the CMA to

investigate small transactions that could not otherwise be considered based on the acquired party's UK turnover.[8]

Indeed, the CMA has been increasingly inclined to investigate and intervene in international mergers whose centre of gravity is not the UK. As part of this, the CMA is also taking a more liberal approach to its share of supply test, with the CMA finding that it had jurisdiction over *Sabre/Farelogix* (2020) based on the share of supply to a single customer (British Airways) and travel agents, despite Farelogix having no travel agent customers in the UK (the CMA argued that Farelogix's services were two-sided, thereby indirectly serving travel agents).[9] (This case has been appealed to the CAT.) Similarly, in *Roche/Spark*, the CMA found jurisdiction based on GT Hem A treatments at Phase 2 (or more advanced) of the clinical development cycle, despite no current sales of that treatment in the UK.[10] *Google/Looker* (2020) is also a reminder that the CMA can find that the share of supply test can be satisfied if the description of goods or services adopted does not correspond with an economic market.[11] In this regard, the CMA's consultation on its revised guidance on its jurisdiction and procedure, which was published on 6 November 2020, emphasises its discretion and the broad scope of its various jurisdictional criteria as to how it defines material influence, what constitutes an enterprise, and its application of the share of supply test.

Moreover, at the end of 2020, the "one stop shop" for mergers under the EUMR, under which the EC had exclusive jurisdiction to assess all mergers involving the UK and all other Member States that fall for consideration under the EUMR (subject to referral mechanisms), will come to an end. After this, the CMA will investigate the UK aspects of all such mergers, including where the markets affected extend beyond the UK.

The remainder of this chapter considers the latest CMA merger statistics, highlighting the recent trend towards more intervention and two exceptions to this trend, namely *Unite/Liberty* and *Inspired/Novomatic*.

2 Recent Trends in UK Merger Control

Overview of CMA merger statistics

High-profile decisions (such as the prohibition of Sainsbury's proposed merger with Asda in 2019,[12] as well as Phase 2 reference decisions that led to the abandonment of the transaction (e.g. *Thermo Fisher Scientific/Roper Technologies*[13] and *TopCashback/Quidco*[14])) often dominate the headlines surrounding the CMA's merger control decisions. However, the CMA makes upwards of 50 Phase 1 decisions and up to a dozen Phase 2 decisions each year, and it is thus appropriate to consider the full breadth of CMA decisions and what this reveals as regards intervention trends.

Table 2.1 below shows the most recent statistics available to 30 September 2020.

Table 2.1: Trends in CMA Phase 1 decisions in relation to qualifying mergers (1 April 2004 – 30 September 2020)

Date	Number of decisions	Cases with CRM (%)	Cases referred (%)	Cases referred + UIL (%)
2004/05	126	28%	14%	18%
2005/06	141	26%	12%	16%
2006/07	106	28%	12%	19%
2007/08	96	23%	10%	16%
2008/09	71	41%	11%	20%
2009/10	62	35%	11%	19%
2010/11	59	36%	14%	20%
2011/12	79	38%	11%	18%
2012/13	77	42%	18%	31%
2013/14	53	36%	15%	15%
2014/15	72	33%	8%	13%
2015/16	60	40%	18%	33%
2016/17	56	50%	9%	25%
2017/18	62	48%	15%	34%
2018/19	54	46%	20%	24%
2019/20	58	40%	22%	33%
2020/21*	18	67%	39%	50%

Source: CMA Merger Outcome Statistics as at 9 October 2020.
* Financial year ("FY") 2020/21 based on first six months (April – September 2020).
UIL = undertakings *in lieu*.

There are several findings from the above table that are worth highlighting. First, FY2020/21 is on track to see the highest proportion of qualifying mergers being reviewed at a CRM *and* the highest proportion of qualifying mergers being referred or only cleared subject to undertakings *in lieu* of reference since UK merger statistics started to be published in April 2004.[15] In the first six months of 2020/21, the CMA reviewed 67 per cent of all qualifying cases at a CRM and three quarters of these were either referred or only cleared subject to undertakings *in lieu* of reference (totalling 50 per cent of all qualifying cases). This is in contrast to 2004/5 to 2014/15 where at most 20 per cent of all qualifying mergers were referred or cleared subject to undertakings *in lieu* of reference in all years bar one (2012/13).

Second, looking back over the last five years, the CMA is now reviewing consistently more than 40 per cent of qualifying mergers at a CRM, compared with less than 40 per cent over the seven preceding years. A deeper look at the CRM cases since 1 April 2017 (through to 30 September 2020) reveals that the CMA found an SLC in 69 per cent of these cases (an increase from 63 per cent over the preceding seven years), with 44 per cent of these cases being referred to Phase 2.

Third, the number of cases that the CMA is referring through to Phase 2 has increased significantly, averaging between 10 and 20 per cent per year until 2018/19, but subsequently increasing to 39 per cent in the first six months of 2020/21.

The increase in the proportion of cases referred or cleared subject to undertakings *in lieu* of reference might be explained to some degree by the mix of cases that the CMA has had to assess. As shown above, the number of CMA decisions per year as regards qualifying mergers has decreased significantly since FY2004/05, reflecting trends in overall M&A activity[16] but also possibly due to an increased focus on higher risk cases. Nevertheless, the more recent developments (from FY2016/17) support our view that the CMA is becoming more inclined to reach SLC findings at Phase 1. This view is also supported by our experience and conversations with other practitioners.

The net result is that since 1 April 2017, 33 per cent of all qualifying mergers are either referred to Phase 2 (21 per cent) or cleared subject to undertakings *in lieu* (12 per cent), compared

with 22 per cent over seven years from April 2010 (13 per cent references and 9 per cent undertakings *in lieu*).

Moreover, notwithstanding the increase in the proportion of qualifying mergers being referred over the last three years, the proportion of these mergers that are cleared unconditionally at Phase 2 has fallen to 36 per cent since 1 April 2017, compared with 48 per cent over the preceding seven years.

However, the fact that the CMA is taking a closer look at an increasing number of mergers during Phase 1 (in the form of CRMs) and at Phase 2 does not mean that potentially problematic mergers cannot be cleared at Phase 1. Our recent experience in two Phase 1 decisions, both of which were unconditionally cleared after a CRM, suggests that the CMA is willing to engage with the parties and their advisors provided that cohesive economic evidence can be put forward. These cases will be explored in sections 3 and 4 below, with a focus on the type of economic evidence that was pivotal to clear the merger.

The (ir)relevance of competitive dynamics

Between 1 April 2010 and 31 March 2020, the Office of Fair Trading ("OFT")/CMA have now made 630 merger decisions at Phase 1 (excluding those mergers found not to qualify). Through our own in-depth analysis of these decisions, we can also examine the relevance of competitive dynamics. In particular, customers may not be adversely affected if barriers to entry and expansion are low, or if they will have sufficient countervailing buyer power. In addition, in a few cases, the exit of one of the parties may be inevitable if it is failing, such that a loss of competition would occur in any event. However, it is clear that compelling evidence is required at Phase 1 for these considerations to lead to a merger being cleared.[17]

The OFT/CMA have considered arguments relating to barriers to entry and expansion in 397 of their 630 Phase 1 merger decisions between 1 April 2010 and 31 March 2020. In the vast majority of these cases (58 per cent), the OFT/CMA did not need to conclude as the merger was cleared for other reasons. In only 19 cases (5 per cent) were the arguments accepted. A detailed review of these 19 cases suggests that entry/expansion arguments may play a supporting role in clearance decisions, but there are still some examples where particularly compelling evidence on entry/expansion has been key to the OFT/CMA's Phase 1 clearance decisions.

In 189 cases, the OFT/CMA considered the extent of countervailing buyer power, but in 56 per cent of cases, there was no need to conclude as the merger was cleared for other reasons. However, where the OFT/CMA did conclude, in only 12 cases (7 per cent) were arguments as to customers' buyer power accepted.[18] Interestingly, there have been no acceptances of countervailing buyer power as a decisive factor to clear a merger since *Flogas/Macgas* in early 2013, potentially reflecting greater caution on the CMA's part at Phase 1 as to the ability of powerful customers to safeguard their interests if they have few alternative suppliers. In this regard, it is important to appreciate that mergers may also reduce customers' buyer power by reducing the number of suppliers to whom they can threaten to switch, and not all customers may have sufficient buyer power.

The final element of competitive dynamics is whether the exiting firm argument applies, which depends on the imminent exit of one of the parties' businesses, the absence of alternative purchasers for the business or assets in question, and a consideration of competitive conditions following any such exit. The OFT/CMA have considered this issue in 74 cases between 1 April 2010 and 31 March 2020. However, the exiting firm argument has been accepted in only seven cases (9 per cent of the cases where these arguments are advanced).[19] These few cases confirm the OFT/CMA's stated position of cautiously assessing the merger against the prevailing conditions of competition if any real doubt or uncertainty remains as to whether the exiting firm argument applies.[20]

The flip side of this is that the CMA increasingly considers carefully whether the counterfactual to the merger is one of the parties becoming a more important competitor (for example, due to its entry or expansion into a market where the other party is a major supplier), such that the loss in competition may be greater than reflected by prevailing competitive conditions. This issue has been a key feature of a number of recent cases, including *Amazon/Deliveroo* (2020) and *Sabre/Farelogix* (2020). This issue was also considered by the CMA in *Inspired/Novomatic*, which is discussed in section 4 below.

3 *Unite/Liberty* (Student Accommodation)

The acquisition by Unite Group plc ("Unite") of Liberty Living Group plc ("Liberty")[21] required the CMA to get to grips with a sector that it had not analysed before. Both companies were active in the supply of purpose-built student accommodation ("PBSA") to full time higher education students seeking accommodation ("FTSSA") at higher education institutions ("HEIs").[22] While the transaction was eventually cleared at Phase 1 – despite customer complaints – this was only after considerable engagement between the CMA and the parties and discussion of the transaction at a CRM in October 2019.

National competitive effects

Before addressing market definition, as is customary in cases involving local service providers, the CMA considered the competitive effects of the merger both nationally and locally. At the national level, the merger clearly did not raise any appreciable national competition concerns as the merged entity's market share would only increase by 8 percentage points to 25 per cent. There were also many other sizeable established rivals with a presence across multiple cities (although the merged business was the largest).[23]

In any event, it is not obvious why national market shares were of any competitive relevance. This is because the CMA accepted that HEIs and students choose local suppliers, and prices are set locally. Moreover, the CMA noted that only 7.4 per cent of the parties' direct consumers identified brand as a reason for choosing the parties and many HEIs offer nomination contracts to smaller suppliers active only in certain cities.[24] Whilst the CMA also considered the parties' market positioning as mid-market operators and that competition in site acquisition/development occurs nationally,[25] such competitive decisions still occur in local markets and there are no HEIs or students that procure student accommodation nationally. In other words, if the merged entity were to worsen its offering, it would lose market share within the local areas where it competed, such that any competitive effects of the merger would be comprehensively addressed by considering the local overlaps.

Local competitive effects

The more complex issues in this case related to the assessment of local competitive effects, which required a consideration of product and geographic market definition, the appropriate market share thresholds to identify those areas where *prima facie* competition concerns might arise, and a detailed assessment of competitive effects in these specific overlapping local areas.

Product market definition

By way of background, there are two categories of customers: HEIs; and FTSSA. HEIs procure accommodation (particularly to meet their student accommodation guarantees) from a mixture of their own accommodation and third-party corporate PBSA. In addition, HEIs have a strategic interest in good quality and value accommodation being available to students as this is a major element of the cost of attending university. Some HEIs also promote houses in multiple occupancy (or "HMO") as an alternative to PBSA on their websites. Students directly let accommodation from HEI providers, corporate PBSA, HMO, and some choose to travel from their homes instead.

The parties argued that all types of accommodation available to students – whether provided by corporates (corporate PBSA), HEIs (HEI PBSA) or private landlords (HMO) – should be included in the product market.[26]

The CMA disagreed, noting that many HEIs are themselves customers (rather than competitors) of corporate PBSA providers, with HEIs sourcing beds from corporate PBSA providers for their own students that cannot be met from their own PBSA stock.[27] These observations are reasonable, but HEIs' options of self-supply would at least appear to be a source of buyer power and reduce their dependence on corporate PBSA.

In addition to these observations, the CMA also cited evidence from its student survey sent only to direct let students, which it interpreted as indicating limited demand side substitutability between PBSA provided by HEIs and corporates. In particular, the survey indicated that nationally the parties' direct let students indicated that if the relevant party's accommodation had been fully booked, "only" 21 per cent would have rented a room in an HEI PBSA property. Nonetheless, the CMA accepted that HEI PBSA may be an alternative to direct let customers who qualify for HEI accommodation guarantees.[28]

With regards to HMO, the CMA also stressed that this type of accommodation may not be suitable for a HEI seeking to enter a nomination agreement, and not a suitable substitute for first year students as they are typically unfamiliar with the city and live away from home for the first time. The CMA also cited its survey of direct let students, which indicated that if the relevant party's accommodation had been fully booked, "only" 24 per cent would have rented a room in an HEI PBSA property.[29]

The CMA thus settled for a narrow frame of reference based on corporate PBSA only. Nevertheless, the parties managed to convince the CMA to take account of competitive constraints imposed by HMO and HEI PBSA in individual areas (more on this below). In this regard, it should be noted at the outset that the CMA's survey of the parties' direct let students indicated that many students would respond to the relevant party's accommodation being fully booked by choosing instead HEI PBSA, HMO and (a lower percentage) travelling from home instead. In short, "out of market" constraints were material, and (as discussed below) these were taken into account by the CMA in its assessment of local competitive effects.

Geographic market definition for local effects

The definition of the geographic scope proved to be an interesting issue in the merger inquiry. While the parties had argued for a local area assessment on a city-wide basis, the CMA opted for much narrower catchment areas, as discussed below.[30]

Practitioners with experience in retail mergers will be familiar with the CMA's approach to local area analysis. Catchment areas are defined based on travel distances – typically driving distances (as consumers generally drive) – from each of the parties' stores. If customers fall in the catchment area of two or more stores, the stores are said to overlap in a local area.

The CMA adjusted this approach to local area analysis to the specific characteristics of the student accommodation market. Instead of basing catchment areas centred around PBSA properties, the CMA used individual HEI campuses as the focal point for its analysis, based on the premise that students and HEIs would only choose accommodation in close proximity. Where both parties had properties within 20 or 30 minutes' walking distance of a specific HEI campus (discussed further below), the parties were said to overlap in the local campus area, and shares of supply were then calculated.[31] As many campuses were located in the same city, this meant that the same properties could overlap in different HEIs' catchment areas.

Before proceeding further, it should be noted that the CMA's approach to market definition meant that it was necessary to calculate walking distances around all HEI campuses, then calculate market shares based on 20 and 30 minutes' walking distances for all of the parties' PBSA, consider the impact of new properties that were committed to open shortly (whether by the parties or third parties), and to check details on the parties' and competitors' accommodation in terms of their locations and number of beds. This was a substantial task that needed to be completed quickly across all the overlapping cities and centred around each overlapping HEI, but fortunately this was made straightforward by AlixPartners' Digital team producing automatically all of these calculations, market share tables (with distances to the overlapping HEI) and maps.

The CMA justified its definition of walking distance catchment areas (as opposed to, for example, public transport or driving distances) around campuses based on findings from its student survey as well as evidence from HEI accommodation managers, competitors and (some) internal documents.[32] The parties objected to such a narrow geographic scope, but the CMA proceeded with the narrow catchment areas as a first step on a "cautious basis".[33]

Nevertheless, competitor properties outside the narrowly defined catchment areas were eventually considered in individual cases. For example, the CMA acknowledged that corporate PBSA properties in Fallowfield – a student neighbourhood in the south of Manchester – impose a constraint on the parties despite the relatively long walking distance to Manchester's largest HEIs.[34] Evidence put forward by the parties, which showed the prevalence of other modes of transport (*inter alia*, high frequency bus services), the geographical dispersal of students staying in accommodation further away and the existence of HEI PBSA in the area, sufficed to convince the CMA in this case.[35] In other local areas, a detailed analysis of actual travel and living patterns and the position of HEI PBSA were also instrumental in convincing the CMA that out of (geographic) market constraints should be taken into account.[36]

***Prima facie* filters and further analysis**

As usual in investigations with numerous local overlaps, the CMA used a filter to identify those areas where a closer look would be warranted.[37] All local areas where the parties' total share of supply and increment exceeded 30 per cent and 5 per cent respectively in either of the catchment areas (20 or 30 minutes' walking distance) were flagged as "failing" the filter.[38] A total of 14 campus catchment areas across 12 HEIs and eight cities were identified based on this approach.

Before proceeding further, it should be noted that these are cautious market share filters (particularly bearing in mind the evidence of out of market competition from other types of accommodation and accommodation further afield), but they were not used to identify SLCs but only local overlaps that warranted further investigation.

The local areas around campuses in Aberdeen and Birmingham were identified by the CMA as unproblematic *before* the CRM due to the specific circumstances in these areas.[39] Interestingly, the parties' combined share of corporate PBSA supply in Aberdeen was higher than in any other city. Nevertheless, the parties managed to convince the CMA through the early provision of additional location-specific evidence before the Issues Paper was written that there was no realistic prospect of an SLC in Aberdeen[40] or Birmingham.[41] In particular, as regards Aberdeen, the sharp decline in the oil price in 2014 had resulted in a sharp increase in the supply of high quality HMO (as workers in the oil industry left), which in turn had a knock-on effect on the demand for corporate PBSA. These empirical findings were confirmed by third parties, including HEIs who noted that they had excess capacity in their own student halls.[42]

The 12 remaining campuses were subject to a detailed assessment by the CMA covering shares of supply, closeness of competition (e.g. differentiation based on pricing and room types), the availability of suitable alternative providers and the relevance of out of market constraints. The CMA also emphasised that its assessment was also conditioned by the price sensitivity of students, which reduced its competition concerns. The parties made detailed submissions with regards to each local area in writing and during the CRM.

Conclusion

In the end, despite third-party complaints in multiple areas, the CMA concluded that the merger did not raise the realistic prospect of an SLC in any of the local areas and cleared the merger unconditionally. This demonstrates that coherent economic evidence can influence decision making at Phase 1.

The transaction is also of interest as it was the first time that the CMA had to consider the impact of a merger between PBSA providers. It is likely that the CMA will follow a similar approach in other cases, and thus a detailed analysis of shares of supply by campus catchment area will need to be prepared by the parties or their advisors.

4 *Inspired/Novomatic UK* (Gaming Machines)

The CMA found itself in more familiar territory with regards to Inspired Entertainment Inc.'s ("Inspired") acquisition of certain business owned by Novomatic (UK) Limited ("Novomatic UK").[43] The parties were both active in the supply of gaming technology and gaming content to regulated lottery, betting and gaming operators. The CMA limited its analysis to two areas of horizontal overlap, namely the supply of B3 gaming machines and the supply of maintenance and servicing of Self-Service Betting Terminals ("SSBTs").[44] A third overlap in the supply of gaming content was identified, but the CMA did not believe that the merger raised *prima facie* concerns in relation to this frame of reference and did not analyse in detail the competitive effects of the merger in this market, noting, *inter alia*, that the parties' combined market share was below 10–20 per cent and Inspired did not supply gaming content to third parties.[45]

As in the case of the *Unite/Liberty* transaction, significant economic evidence was considered as part of the Phase 1 inquiry. Evidence was provided both in writing as well as orally during a CRM. Eventually the CMA cleared the transaction unconditionally despite the overlaps mentioned above and customer complaints.

In the remainder of this section, we summarise the most interesting aspects of the CMA's decision, focusing on the approach to market definition in the supply of gaming machines, the measurement of shares of supply, and the assessment of vertical effects.

Revised frame of reference in light of regulatory changes

As mentioned above, the CMA was already familiar with the industry and, in normal circumstances, it thus could have relied on its previous decisions to define the markets and carry out its competitive effects analysis. Instead, it demonstrated a willingness to reconsider earlier approaches to market definition.

In particular, the preceding OFT decision in 2012 in *AGL/Danoptra* assessed competitive effects both in the supply of all gaming machines and, separately, in each of the categories of gaming machines where the merging parties overlapped.[46] Machines are categorised by the Gambling Act based on maximum stakes and prize available (in decreasing order: B1, B2, B3, B4, C & D).[47] The category determines whether and how many machines a certain venue can place on its floors. For example, Bingo halls can only stock B3 – D machines, while Betting Shops (also known as Licensed Betting Offices or "LBOs") are allowed a maximum of four higher stake B2 machines per premise.

However, a recent regulatory change in the market – the Triennial Review – led to a revision of the CMA's approach to market definition. As a result of the Review, the stakes for B2 gaming machines were reduced from £100 to £2 in line with B3 gaming terminals.[48] B2 and B3 machines thus became effectively equivalent, a development that increased substitutability between machine types and, according to the CMA, led to a convergence of the B2 and B3 markets.

This consolidation of the frame of reference did not play out in the parties' favour. This is because if there were separate markets this would have reduced the overall overlap in the parties' businesses, because Inspired was predominantly active in the supply of B2 machines to LBOs, while the target companies focused on the supply of B3 machines to other customer segments and did not have a B2 offering.[49]

Nevertheless, the CMA did not believe that – absent the transaction – the target companies would have started to compete with Inspired for customers who previously bought B2 machines (predominantly LBOs).[50] Consequently, the consolidation of the frame of reference had no material impact on the outcome of the analysis with regards to this customer segment.

Measuring shares of supply in a market with different distribution models

The measurement of the shares of the supply within the gaming machine market was an area of controversy and was much debated both in writing and during the CRM. The issue was complicated due to the existence of different distribution models (with different ownership structures and payment terms) between machine suppliers. Further, the current shares of supply, which were necessarily calculated using historical data, did not yet account for the anticipated impact of the Triennial Review and the potential for a more competitive counterfactual (i.e. increased competition in future between the parties, following the Triennial Review).

The CMA initially looked at: (a) 2018 revenue shares; and (b) shares of the installed base (independently of when the gaming machine was manufactured or supplied to the venue).[51] The parties disagreed, noting that these measures would overstate the competitive strength of certain businesses and ignore the effects of the Triennial Review on the market.[52]

In particular, Inspired and one of its main competitors (Scientific Games) mostly operated on a revenue sharing basis rather than selling machines outright. As these agreements cover the cost of the machine as well as other services such as the provision of gaming content, an unadjusted comparison to revenues from outright machine sales (where the customer must procure its own gaming content and service the machine) would not have been appropriate. Share of supply based on revenues from the deployment of machines would thus have overstated the importance of Inspired and Scientific Games.

Further, both Inspired and Scientific Games historically focused on the LBO segment, where the high-stakes B2 gaming machines used to generate much higher revenues than B3 machines, which were common in other customer segments (e.g. bingo halls). As the Triennial Review lowered the stakes on B2 machines (from £100 to £2), revenues per machine were expected to converge across customer segments over time (i.e. revenues in the LBO segment, where Inspired had a historical advantage, were expected to fall). Historical market shares based on pre-Triennial Review revenues would thus have been a poor indicator of Inspired's competitive strength in the years following the transaction.

Finally, the Triennial Review was expected to make B2 machines less attractive for LBOs, who had already started to close shops as a result. Consequently, any calculation based on the number of historically installed machines would have overstated the importance of LBOs as a customer segment.

While the CMA did not agree with all arguments put forward by the parties, it did settle for a different approach based on the share of installations of new gaming machines over a three-year period.[53] The decision notes that this measure is the "*most appropriate indicator of rivalry in the circumstances of this case*" given that revenues from legacy installed base are excluded while addressing the issue of the lumpiness of supply (new installations can fluctuate substantially from one year to another).

Overall, the CMA concluded that there was no realistic prospect of an SLC as a result of unilateral horizontal effects in relation to both the supply of B3 gaming machines overall and to each customer segment separately.[54] This was due to the presence of other large competitors post-merger, including the business retained by Novomatic, such that the merger would not materially increase overall market concentration. Indeed, Novomatic's market share in B3 machines *pre-merger* (including the target and retained business) would be similar to the merged entity's market share *post-merger*. Looking at specific B3 customer segments, the parties did not currently overlap as regards LBOs, Novomatic's *pre-merger* market share in the supply of B3 machines to adult gaming centres was greater than the merged entity's share and this was similarly the case as regards adult gaming machines and bingo halls combined.

In this regard, it was particularly important for the CMA to accept that Novomatic, the historical market leader, would remain a material rival that would compete effectively post-merger, rather than exiting the market. Here, Inspired was able to demonstrate that Novomatic's decision to retain certain businesses had reduced the purchase price for the transaction, and Novomatic was also able to provide the CMA with detailed evidence on its plans to compete with Inspired post-merger.[55]

The CMA also considered the competitive effects of Inspired expanding its sales of B3 machines to adult gaming centres and bingo halls, with the merger counterfactual being that competition would have increased in absence of the merger. Nonetheless, the CMA considered that there would not be any material difference in competition in the counterfactual and post-merger: "*In both cases, there would be four significant suppliers competing to supply customers with shares of supply that are broadly similar under either scenario.*"[56] Crucial to this conclusion was the CMA's finding that Novomatic's retained business would be an effective competitor.

With regards to unilateral effects in the provision of maintenance and servicing SSBTs, the CMA found that the merged business' market share would increase by 5–10 per cent to 70–80 per cent and the transaction reduced the number of competitors from four to three (with Scientific Games only providing these services to William Hill). This was arguably a *de minimis* market as its size was less than £5 million, but the CMA reached no conclusion on this point. However, the CMA still found no SLC on the basis that the parties are not close competitors and other alternatives could emerge in the near future as barriers to entry are low (the CMA accepted that any engineering firm with access to personnel could carry out these services).[57] Accordingly, this case is also noteworthy in that the CMA's clearance decision was in part based on the conclusion that barriers to entry were low. This clearance decision was no doubt assisted by the fact no LBO raised any concerns as regards these services.

Assessment of vertical effects

The CMA further considered whether the merger could lead to an SLC through vertical effects, namely by foreclosing rival gaming content providers who previously supplied gaming content for Inspired machines.[58] Inspired historically used its own as well as third-party gaming content on its machines and allowed customers to purchase their own gaming content if they wished to do so. As such, Inspired's machines were a route to market for gaming content providers who compete with both Inspired and Novomatic. As usual, the CMA thus assessed whether the merged entity would have the (a) ability, and (b) incentive to foreclose rival gaming content providers, and (c) whether such a strategy would have a detrimental effect on competition.[59]

With regards to Inspired's ability, the CMA found that the only significant gaming content provider who relied on Inspired pre-merger and did not have an alternative route to market was William Hill (itself also a large operator of LBOs), and the CMA also found that Inspired may not be able to foreclose access to a large share of its installed base for contractual reasons. All other major providers were themselves manufacturers of B3 gaming machines and thus not reliant on Inspired. The CMA thus considered that the merger was unlikely to provide Inspired with the ability to foreclose rival gaming content providers.[60]

The CMA did not have to reach a definite conclusion with regards to Inspired's ability to foreclose rivals, because the evidence with regard to its incentive was sufficiently clear. Economic analysis put forward by the parties – corroborated by views from third parties – showed that the likely benefits of foreclosing rival content providers would be outweighed by the associated costs. In summary, the following points were important to the CMA's findings:[61]

- the cost of gaming content supplied by providers who relied on Inspired as a route to market was dwarfed by Inspired's machine manufacturing revenues;
- a deterioration in gaming content would make Inspired's machines less attractive, leading to a reduction in gaming machine revenues; and
- the gaming content acquired through the transaction from Novomatic UK was insufficient to maintain the attractiveness of Inspired's machines.

Consequently, the CMA found that the merger did not give rise to a realistic prospect of an SLC as a result of vertical effects in relation to the supply of gaming content.[62]

Conclusion

As in *Unite/Liberty*, the CMA cleared the transaction unconditionally at Phase 1. This is despite the CMA changing its approach to market definition, a complicated debate about the correct measurement of shares of supply in an evolving market, and the presence of a vertical theory of harm. This goes to show that coherent economic evidence that allows the CMA to gain a good understanding of the impact of the merger on the parties' incentives is crucial for a successful Phase 1 clearance.

Endnotes

1. The authors acted for the merging parties on these cases, led by Herbert Smith Freehills LLP and Addleshaw Goddard LLP, respectively. We are grateful for the comments of Bruce Kilpatrick, Head of Competition at Addleshaw Goddard.
2. Enforcement orders can also be imposed in relation to proposed transactions. The CMA's guidance indicates that it may impose an enforcement order in relation to an anticipated merger where: for example, commercially sensitive information is being exchanged between merger parties; the parties intend to, or are already, integrating their businesses; the merger parties have begun to conduct jointly commercial negotiations with customers or suppliers; and key staff have begun to leave the target business or are likely to do so. Whilst not mentioned in its guidance, analogous concerns might arise if customers were to leave the target business.
3. In addition, on 22 April 2020, the CMA published a "refresher" of its position on mergers involving failing firms ("the CMA's Refreshed Guidance"), which is available at: https://www.gov.uk/government/publications/merger-assessments-during-the-coronavirus-covid-19-pandemic/annex-a-summary-of-cmas-position-on-mergers-involving-failing-firms. The CMA's Refreshed Guidance emphasises that there are real execution risks for both sellers and buyers associated with mergers involving failing firms if these otherwise raise competition issues. One aspect of these risks that the CMA chose to particularly highlight in the context of completed mergers is that the CMA's initial enforcement orders require the acquirer to provide sufficient resources to the target to enable it to operate on the basis of its pre-merger business plan. This raises the real concern as to whether this amounts to an obligation on the purchaser to write a blank cheque, and to keep a flailing firm on life support for the duration of a forced sale process should the CMA reach an adverse finding. The application of the failing firm defence is considered further by Mat Hughes and John Bruce in a chapter published in *Global Legal Insights – Merger Control 2020* (July 2020), which is available at: https://www.globallegalinsights.com/practice-areas/merger-control-laws-and-regulations/1-covid-19-avoiding-the-failure-of-the-failing-firm-defence.
4. See: https://uk.practicallaw.thomsonreuters.com/w-027-2175?transitionType=Default&contextData=(sc.Default)&firstPage=true.
5. Penalties have been imposed for breaches of enforcement orders, including on: Electro Rent (£100,000 and a further £200,000 penalty); European Metal Recycling (£300,000 penalty); Vanilla Group (£120,000 penalty); PayPal/iZettle (£250,000 penalty); and JD Sports (£300,000 which has been withdrawn following appeal to the CAT, and at the time of writing the CMA is reassessing its position as regards this fine). The CMA appears to have increased its use of such fines since the first time it imposed a fine for breach of an enforcement order on Electro Rent in 2018. The CMA can impose penalties of up to 5 per cent of global turnover, and whilst the CMA's fines have been less than this to date, its 2019 guidance warns that: "*The CMA will … impose proportionately larger penalties in future cases should this prove necessary in the interests of deterrence.*"
6. Most recently, the CMA fined Amazon £55,000 for failure to provide complete responses to two statutory information requests (totalling 189 documents submitted up to two months after the deadline). It has also imposed fines on Hungryhouse, AL-KO Kober, Rentokil Initial, and Sabre Corporation. Whilst the maximum fine the CMA can impose for non-compliance with a Section 109 Notice is £30,000, it is important to appreciate that the CMA expects good faith cooperation with its investigations. The CMA's 2019 reform proposals suggested that the CMA might seek greater power to impose fines for non-compliance with information requests. As regards document requests, it would be prudent not to carry out manual document searches, but instead to use electronic e-discovery tools that can confirm that all documents held by identified custodians have been searched against. This is because manual searches tend to be incomplete and time-consuming, and it is easy to miss custodians if documents/data are stored on different IT systems.
7. These descriptions are meant to be high-level, not a detailed review of EC or UK merger control.
8. A good review of these cases is provided by an article by Miranda Cole and Rolf Ali of Covington, available at: https://www.covcompetition.com/2020/08/the-cmas-approach-to-jurisdiction-in-recent-merger-cases/.
9. For further discussion on these cases, see: https://www.linklaters.com/en/insights/blogs/linkingcompetition/2020/january/casting-the-net-wider-three-themes-from-the-cmas-jurisdictional-skirmishes-in-2019.
10. See: https://assets.publishing.service.gov.uk/media/5e3d7c0240f0b6090c63abc8/2020207_-_Roche_Spark_-_non-confidential_Redacted-.pdf.
11. *Completed acquisition by Google LLC of Looker Data Sciences, Inc.*, https://assets.publishing.service.gov.uk/media/5e6f8119e90e070ac9b21395/Google_Looker_decision-.pdf (see paragraph 54). On the facts of the case, the CMA found that the parties were both active in the supply of BI tools, but that few customers identified Google's services as an alternative to Looker's BI tool (see paragraphs 86, 105–106 and 109).
12. *Anticipated merger between J Sainsbury PLC and Asda Group Ltd*, https://www.gov.uk/cma-cases/j-sainsbury-plc-asda-group-ltd-merger-inquiry.
13. *Anticipated acquisition by Thermo Fisher Scientific Inc of Gatan*, https://www.gov.uk/cma-cases/thermo-fisher-scientific-roper-technologies-merger-inquiry.
14. *Anticipated acquisition by Top Online Partners Group Limited of Maple Syrup Group Limited and its Subsidiaries*, https://www.gov.uk/cma-cases/topcashback-quidco-merger-inquiry.
15. Referrals are measured as the share of all qualifying decisions (i.e. all decisions excluding those where the CMA found that the transactions did not qualify as a relevant merger situation). The exclusion of mergers found not to qualify is to provide a consistent set of statistics on the CMA's substantive assessment of mergers as such decisions are have become rare since 2015 due to the pre-notification process.

16. The Law Society hosted an excellent session on 4 June 2020 given by Colin Raftery (Senior Director of Mergers at the CMA) and Anna Caro (Assistant Director of Mergers at the CMA) on "CMA merger control during the pandemic". This also highlighted the strong link between overall M&A activity and UK merger filings and how both were adversely affected by the Financial Crisis. (Available at: https://webinar.lawsociety.org.uk/playback/presentation/2.0/playback.html?meetingId=89b6fbeaf4a513b7b63833d71521f56f2f1f5278-1591273170519.)
17. See, for example, *Ballyclare/LHD* (2014), *Web Reservations International/Hostelbookers.com* (2013), or *Tulip/Easey* (2017). (AlixPartners acted for the parties on *Ballyclare/LHD* (2014)).
18. See, for example, *Unifeeder/Feederlink* (2012).
19. See, for example, *Sports Direct/JJB Sport* (2012) or *Aer Lingus/City Jet* (2018).
20. The application of the failing firm defence is considered in detail in the chapter referred to in note 3.
21. ME/6825/19 *Anticipated acquisition by Unite Group plc of Liberty Living Group plc*, https://www.gov.uk/cma-cases/unite-group-plc-liberty-living-group-plc-merger-inquiry.
22. *Unite Group plc / Liberty Living Group plc merger inquiry*, CMA clearance decision of 13/12/2019, paragraph 3. Available here: https://assets.publishing.service.gov.uk/media/5df27587ed915d09360e5457/unite_liberty_final_decision.pdf.
23. *Ibid*, paragraph 111.
24. *Ibid*., paragraphs 98, 105–106.
25. *Ibid*., paragraphs 101–102 and 107–108.
26. *Ibid*., paragraph 56.
27. *Ibid*., paragraph 62.
28. *Ibid*., paragraphs 60–65.
29. *Ibid*., paragraph 68.
30. *Ibid*., paragraphs 79 & 90.
31. *Ibid*., paragraph 126.
32. *Ibid*., paragraphs 83–88.
33. *Ibid*., paragraph 89.
34. *Ibid*., paragraph 233. Manchester's largest HEIs in terms of FTSSA are the University of Manchester and Manchester Metropolitan University.
35. *Ibid*., paragraph 232.
36. *Ibid*., paragraphs 173–174 (Leicester) and 212–213 (London). In addition, for a number of the parties' properties that were within a 20 or 30 minutes' walking distance of an overlapping HEI, all or the majority of the students actually staying in these properties were in fact attending a different HEI. For example, this was the case for one or both of the parties' properties near the King's College London and Queen Mary University of London campuses (see paragraphs 196–197).
37. *Ibid*., paragraph 127.
38. *Ibid*., paragraph 128.
39. *Ibid*., paragraph 132.
40. *Ibid*., paragraphs 133–134.
41. *Ibid*., paragraphs 135–136.
42. *Ibid*., paragraph 133.
43. ME/6824/19 *Anticipated acquisition by Inspired Entertainment Inc. Of certain business owned by Novomatic (UK) Limited*, available here: https://www.gov.uk/cma-cases/inspired-entertainment-novomatic-uk-merger-inquiry.
44. *Inspired Entertainment/Novomatic UK merger inquiry*, CMA clearance decision of 24/10/2019 (*Inspired/Novomatic*), paragraph 5. Available here: https://assets.publishing.service.gov.uk/media/5db17ea2e5274a0920a53611/inspired_entertainment_novomatic_full_text_decision.pdf.
45. *Ibid*., paragraph 75.
46. ME/5413/12 *Anticipated acquisition by Astra Games Limited of certain gaming machine and related businesses from the Danoptra Group* (2012).
47. See: https://www.gamblingcommission.gov.uk/for-gambling-businesses/Compliance/Sector-specific-compliance/Arcades-and-machines/Gaming-machine-categories/Gaming-machine-categories.aspx.
48. *Inspired/Novomatic*, paragraph 37.
49. *Ibid*., paragraphs 13–14.
50. *Ibid*., paragraphs 32 & 128–131.
51. *Ibid*., paragraph 77.
52. *Ibid*., paragraph 78.
53. *Ibid*., paragraph 80.
54. *Ibid*., paragraph 132.
55. *Ibid*., paragraphs 95–114.
56. *Ibid*., paragraphs 120–125.
57. *Ibid*., paragraphs 134–141.
58. *Ibid*., paragraph 143.
59. *Ibid*., paragraph 144.
60. *Ibid*., paragraphs 147–152.
61. *Ibid*., paragraphs 153–158.
62. *Ibid*., paragraph 161.

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AlixPartners has a multi-disciplinary practice covering economics, forensic accounting, and information management services (such as e-discovery and applied data analytics). The firm also has post-merger integration experts who provide evidence on efficiencies in mergers, and restructuring experts who advise on "failing firm" viability issues. Combined with AlixPartners' industry expertise, this wide-ranging capability allows us to create robust evidence and analysis on the issues that matter most to the case. This included advising on *Liberty/Unite*, *Inspired/Novomatic*, *JD Sports/Go Outdoors*, cleared unconditionally by the CMA at Phase 1, *BT/EE*, which was cleared unconditionally by the CMA at Phase 2, and various Phase 2 EU mergers such as *H3G/O2* (acting for EE) and *Nynas/Shell* (which was cleared unconditionally on the basis of a combination of the exiting firm defence and merger efficiencies). In 2019/20, the firm acted on three UK Phase 2 mergers, namely *Bauer Radio*, *Hunter Douglas/247*, and *JD Sports/Footasylum*. AlixPartners' economics practice also engages in a range of other competition economics work. Members of the team have acted in relation to the European Commission investigations into Visa inter-regional interchange fees, credit default swaps and ebooks, the CMA investigation into retail banking, and market investigations concerning credit information, payday lending and private motor insurance. They are also acting in relation to a range of matters involving competition litigation, such as acting for seven OEMs in relation to truck/car part cartels, interchange fees for Visa Inc., a rail ticketing class action, *Network Rail/Achilles*, the envelopes cartel, the polyurethane foam cartel for multiple claimants, and pay-for-delay pharmaceutical litigation.

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