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Increased Scrutiny for Tech Mergers: What You Need to Know


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Introduction

Despite the coronavirus pandemic during 2021–2022, M&A activity in the tech sector maintained pace with transactions including NVIDIA's (aborted) acquisition of Arm Limited, Broadcom's acquisition of VMware, and Microsoft's acquisition of Activision Blizzard, several of which faced intense regulatory scrutiny.

Deals in the digital space will continue to be in the regulatory spotlight. New rules will grant regulators greater power to intervene in this sector, leading to parties facing multiple reviews by competition authorities across the globe with different timetables and potentially divergent outcomes, including on remedies.

In the 2021 edition of *ICLG – Merger Control*, the Expert Analysis Chapter "*Reform or Revolution? The Approach to Assessing Digital Mergers*" considered issues relating to digital mergers from a policy perspective. It focused on the characteristics of digital platforms, why it may be difficult to assess mergers involving these companies using traditional analytical tools, and four emerging theories of harm relating to digital mergers.

This chapter will consider developments in the last two years; in particular, jurisdictional reforms at a national and EU level and increased use of existing enforcement tools. It also examines the theories of harm that regulators increasingly apply to tech mergers, together with an overview of foreign direct investment ("**FDI**") regimes, which parties need to consider in parallel to merger control regimes.

Jurisdictional Issues: New National and Supranational Reforms – A Comparative Overview

The need for reform

In recent debates, the main concern raised by many regulators has been that significant digital transactions could slip "*under the radar*"[1] (so-called "*killer acquisitions*" – as explained below). The key question here is whether competition authorities can assert jurisdiction over a transaction if: turnover thresholds are not met; there is little or no nexus with the jurisdiction in question; or a product/service is yet to be developed or is in its infancy.

Regulators have taken divergent approaches, and the substantive (or procedural) issues in these cases can be complex. Companies and their advisers must therefore carry out a careful competition analysis of deals in the tech sector at an early stage.

Another long-standing concern has been the perceived under-enforcement[2] of merger control in the digital sector, with *Facebook/Instagram*[3] and *Google/DoubleClick*[4] being oft-cited examples. The concern underpinning under-enforcement is that mergers involving large digital players may undermine innovation and create high barriers to entry (particularly for start-ups) to the detriment of consumers who may pay higher prices or face less choice of products or services. Getting the balance right between over- and under-enforcement will remain challenging for regulators across the globe.

Commentators have questioned whether existing competition tools provide sufficient and adequate protection for potential competition. For example:

(a) Former Chief Executive of the UK Competition and Markets Authority ("**CMA**"), Andrea Coscelli, suggested that an "*inflection point in competition policy*" has been reached and expressed concern that existing tools are "*often too slow to grapple with fast-moving digital markets*".[5]

(b) Speaking in 2022,[6] the European Commissioner for Competition, Margrethe Vestager ("**Commissioner Vestager**"), has emphasised the need for cooperation between competition authorities "*both inside and outside the EU*" when it comes to digital markets.

(c) Former Chair of the Australian Competition and Consumer Commission ("**ACCC**"), Rod Sims, expressed concern that large digital platforms were not just "*true innovators*" but also "*serial acquirers*".[7] He suggested that certain digital transactions should, in hindsight, "*not have been allowed to proceed*" in Australia.[8]

(d) In January 2022, the Federal Trade Commission and Department of Justice in the US launched a review of the US merger guidelines, with the goal of accounting for certain features of digital markets, such as zero-price dynamics, the competitive significance of data and network externalities.[9] Assistant Attorney General Jonathan Kanter of the Department of Justice's Antitrust Division commented that the regulators need to "*think carefully about how to ensure our merger enforcement tools are fit for purpose in the modern economy*".[10]

Publicly expressed concerns have centred on whether, in the digital sector: (i) some mergers that could have raised concerns were not caught by the existing jurisdictional thresholds; or (ii) some mergers were cleared that may have harmed competition. As a result, regulators considered (and in some cases implemented) new tools specifically targeting the digital sector, such as the Digital Markets Act ("**DMA**") in the EU.

In addition, regulators have been making more proactive use of existing tools and asserting jurisdiction over more mergers in technology.

EU reform – the DMA[11]

The EU has enacted the DMA, which will require companies designated as "*gatekeepers*" to notify transactions to the European Commission. The DMA was published in the Official Journal on 12 October 2022 and the provisions will apply from:

(a) 1 November 2022 for Articles 3(6), 3(7), 40 and 46–50, which relate to procedural elements (such as empowering the European Commission to adopt delegated acts, implementing measures and guidance).

(b) 25 June 2023 for Articles 42 and 43, which govern representative actions and whistleblowing.

(c) 2 May 2023 for the remaining articles, including those governing designation as a gatekeeper and the requirement to inform the European Commission of certain merger activity (see further below).

Designation as "*gatekeeper*"

The DMA carries many significant and arguably ground-breaking changes for companies designated as "*gatekeepers*" because they provide so-called "*core platform services*", including search engines, social networks, online marketplaces and web browsers, online advertising services and cloud computing services.

Under Article 3(1) of the DMA, a company shall be designated as a gatekeeper if it:

(i) has a significant impact on the internal market;

(ii) provides a core platform service that is an important gateway for business users to reach end-users; and

(iii) enjoys an entrenched and durable position in its operations, or it is foreseeable that it will enjoy such a position soon.

Article 3(2) states that a company will be presumed to meet these requirements where:

(a) In relation to point (i), it achieves an annual turnover in the EU of at least EUR 7.5 billion in each of the last three financial years, or where its average market capitalisation or its equivalent fair market value amounted to at least EUR 75 billion in the last financial year and it provides the same core platform service in at least three Member States.

(b) In relation to point (ii), where it provides a core platform service that in the last financial year has at least 45 million monthly active end-users in the EU and at least 10,000 yearly active end-users in the EU.

(c) In relation to point (iii), where the thresholds in (b) above were met in each of the last three financial years.

Companies meeting the criteria in Article 3(1) must notify the European Commission within two months and provide the information set out in Article 3(2). The European Commission then has 45 working days to issue a decision designating the company as a gatekeeper. The first designations are expected to take place in September 2023. A plethora of behavioural rules will also apply to gatekeepers six months after the designation takes place (from around March 2024).[12]

It remains to be seen how many companies will actually be designated as gatekeepers in practice – the DMA's recitals do not anticipate a significant number of designations taking place. Importantly, gatekeeper status will not only apply to big digital platforms but also to smaller companies dealing with financial data, for example. Careful scrutiny is thus needed as gatekeepers are subject to additional obligations, including a requirement to notify the European Commission of certain M&A activity, and breaches may be punished by fines.

Transaction notification requirements

From an M&A perspective, under Article 14 of the DMA, companies that have been designated will have to notify the European Commission, in advance, of any proposed transaction that involves another platform provider in the digital sector. The reporting obligation under the DMA falls short of a notification requirement under the merger regime but imposes another compliance requirement which parties must factor into their deal timeline. While the precise form of the notification has not yet been set out, companies will need to provide the European Commission with information on the parties, their activities, the transaction value, the transaction rationale and the Member States concerned by the transaction, as well as the information required under Article 3(2) for any relevant core platform services.

Importantly, this obligation applies to all transactions, irrespective of whether the EU or national merger control thresholds are met. This will, necessarily, substantially increase the number of transactions in the tech sector that are subject to European Commission scrutiny.

The European Commission can share information regarding such transactions with the national competition authorities ("**NCAs**") of EU Member States, meaning that a greater number of transactions in the digital sector will also be visible to the NCAs as well as the European Commission, as information is shared between these authorities. Commissioner Vestager said that this notification requirement "*creates important synergies with the new approach to Article 22 [of the EU Merger Regulation], because the Commission will be in a position, where needed, to invite Member States to refer cases, when the Commission has been informed about a transaction in accordance with the DMA*".[13]

The DMA expressly states[14] that NCAs may use the information provided to request the European Commission to examine the transaction under Article 22 of the EU Merger Regulation[15] ("**Article 22**") (see further below). While it remains to be seen how far this will result in an increased number of transactions being subject to merger control, authorities are already actively monitoring press releases and reporting on potential mergers. The European Commission has proposed hiring 80 additional employees to perform functions under the DMA; however, Members of the European Parliament have raised concerns that "*fulfilment will be seriously jeopardised*" if further additional staff are not hired.[16] It is possible that a far greater number of companies may be caught by the wording of the DMA than the drafters anticipated.

Besides increasing visibility between regulators, designation as a gatekeeper also opens up the opportunity for other digital companies to object to transactions.

Practical considerations for gatekeepers

Companies that may qualify as gatekeepers should consider engaging early with the European Commission to manage risks to the deal timeline. Early engagement with the European Commission is particularly advisable given the lack of guidelines accompanying the DMA (so far). While litigation is anticipated in relation to designations under the DMA, appeals will be long proceedings. In the meantime, companies will need to comply with the notification requirement in Article 14 of the DMA and any victories in litigation may come too late for commercial imperatives.

Companies will also need to consider the appropriate protections that should be built into their transaction documents, particularly in light of gun-jumping proceedings issued in *Illumina/Grail*.[17] Transaction documents typically already contain appropriate provisions where the deal triggers filings before the European Commission or NCAs. These provisions will now need to address the possibility of a referral even where no NCAs have jurisdiction. One possible option would be a provision to automatically extend the long-stop date if there is an Article 22 referral. Alternatively, parties could include a provision triggered by an Article 22 referral that includes a procedure to decide how to allocate risk and the impact on the deal timetable. Break fees will be particularly important in this respect, as companies will doubtless wish to avoid the Hobson's choice of closing before the European Commission has finished its review or paying very substantial break fees in the event of a late or unexpected referral.

The DMA may actually confer additional certainty in this context if authorities take the view that there would be no need to approach the NCAs of all 27 Member States to ensure the transaction has been "*made known*" to the NCA for the clock to start running on the 15-working-day deadline where the European Commission has been informed.

National reforms

A transaction value threshold has been seen as a way for authorities to examine so-called "*killer acquisitions*" of nascent companies that may not yet have any (or substantial) turnover, but that already are or may become significant drivers of innovation. The concern being that such transactions allow the acquirer to "*kill*" the rival's business post-acquisition, reducing competition in the market and depriving consumers of potential benefits.

Germany and Austria

Germany and Austria were early adopters of "*transaction value*" thresholds. Accordingly, transactions below the primary turnover thresholds may still be notifiable if the consideration exceeds EUR 400 million (Germany[18]) or EUR 200 million (Austria[19]) and the target has substantial domestic operations.

The main criterion for assessing "*substantial domestic operations*" is the target's turnover, and whether said turnover adequately reflects the target's market position and competitive potential – this is unlikely to apply in a market not characterised by turnover.[20] In this case, further criteria, such as the number of users of digital services (such as apps) must be assessed.[21]

The assessment of these criteria requires a thorough analysis of the relevant facts and markets in each case, leading to potentially different outcomes by the German and Austrian NCAs.[22]

The UK

In the UK, the government announced that a draft Digital Markets, Competition and Consumer Bill (the "**Bill**") will be published in the 2022/2023 Parliamentary session. The current status of the Bill is uncertain; however, it is not expected to be laid before Parliament until 2023/2024.[23] The Bill would introduce more widespread reforms to competition and consumer law in the UK, as well as a new regime for digital platforms. The current jurisdictional thresholds in the UK would be revised (see the United Kingdom chapter in this *Guide* for further details). In addition, the CMA would be given administrative powers to enforce consumer law in the UK, with the possibility of imposing fines of up to 10% of the company's worldwide turnover. A particular emphasis has been placed on digital markets, including issues such as false or misleading reviews and online exploitation of consumers.

For the new digital regime, the Bill targets companies with a so-called strategic market status ("**SMS**") in specific digital activities. The concept of SMS is similar to the concept of "*gatekeeper*" under the DMA (discussed above). The UK proposals also incorporate a transaction value threshold, meaning companies with SMS will have to notify a transaction where:

(a) the SMS company acquires at least 15% equity or voting share after the transaction;
(b) the value of the SMS company's holding is over GBP 25 million; and
(c) the transaction meets a UK nexus test.

Before completing a transaction exceeding the thresholds, SMS firms would need to report the transaction to the CMA. The CMA would then undertake an initial review of the mergers to consider whether it would warrant further investigation.

Aside from the concept of SMS, the UK has also proposed a new threshold to capture possible killer acquisitions, which would give the CMA jurisdiction where the acquirer has:

(a) an existing share of supply of goods or services of 33% in the UK, or a substantial part of the UK; and
(b) UK turnover of at least GBP 350 million.

Although in this case merger filings would remain voluntary, the CMA's jurisdiction has been broadened. In light of stringent hold separate orders that the CMA can impose, parties will need to consider the need for a UK filing early on in a transaction.

The CMA is showing an increased interest in mergers raising digital issues and has conducted a number of Phase 2 merger reviews, including in cases where the parties had chosen not to make a voluntary filing, such as *Meta/GIPHY*.[24] Where multiple regulators are reviewing a transaction in parallel, the CMA decision is often the final regulatory clearance pending due to the possible length of Phase 2 reviews in the UK. Parties should therefore consider at an early stage in a transaction whether a notification (or at least an approach to the CMA's Mergers Intelligence Committee) would be prudent to avoid last-minute surprises that may derail deal timelines.

Italy

Italy has taken a different approach and, in August 2022, introduced a new *ex post* review power enabling the *Autorità Garante della Concorrenza e del Mercato* to call in transactions that:

(a) meet one of two turnover thresholds (one of which is where the aggregate worldwide turnover of the parties exceeds EUR 5 billion);
(b) raise concrete risks for competition in the national market (or a part thereof), including negative effects on the development of small enterprises with innovative strategies; and
(c) have not been completed for more than six months.

Such *ex post* review processes will reduce deal certainty for companies and require an in-depth risk assessment, as well as consideration of the benefits of proactively contacting the authority to explain the positive aspects of a deal, particularly in high-profile cases.

Jurisdictional Issues: Existing Tools

Referrals to the European Commission using existing mechanisms

Competition authorities in EU Member States are increasingly deploying existing tools to establish jurisdiction, including the referral mechanism whereby NCAs can ask the European Commission to review a transaction that (a) affects trade between EU Member States, and (b) would have a significant impact on competition in the territory of the Member State making the request.[25] The European Commission can also invite NCAs to make a referral.

In a speech in September 2022,[26] Commissioner Vestager stated:

> "*By adapting the referral mechanism, we can capture below-threshold acquisitions that could raise competition concerns. And to maximise this potential, we need to work together with the national competition authorities across the Union to develop a unified and coherent approach.*"

Article 22 was designed to enable Member States without national merger control rules to refer transactions to the European Commission,[27] and with the development of national regimes, the European Commission had discouraged referrals.[28] In contrast to that objective, in March 2021 the European Commission provided guidance[29] encouraging Member States to refer certain transactions that do not meet national merger control thresholds and set out the criteria that it may consider when deciding whether to accept referrals.

Speaking in July 2021, Guillaume Loriot, the European Commission's Deputy Director General with special responsibility for mergers, recalled the driving forces behind this change, noting that the European Commission must make "*no compromise on ensuring that there is no enforcement gap with regard to cases that deserve a review and that could otherwise escape such effective control of concentration*".[30] The European Commission guidance specifically refers to killer transactions in the digital and pharmaceutical sectors, noting that market developments of mergers involving firms that "*play… a significant competitive role… despite generating little or no turnover at the moment of the concentration… appear particularly significant in the digital economy*".[31]

From the European Commission's perspective, using the existing referral mechanism has the advantage of preventing time-consuming and resource-intensive legislative reform of the EU merger thresholds in favour of a more expedient tool. It also offers the European Commission more flexibility to review mergers on a case-by-case basis.

In explaining why turnover-based thresholds may not "*capture all transactions that could materially impact the internal market*", Commissioner Vestager commented that "*with zero-priced markets and business models based on data and early R&D, turnover is not the only signal of competitive significance – sometimes it is not a signal at all*".[32] However, a transaction value threshold akin to the national regimes discussed above may arguably have offered the transacting parties greater certainty about whether the European Commission will be able to review the particular transaction.

Parties currently face significant uncertainty and should seek legal advice early on in a transaction. From a policy perspective, the lack of a clear threshold arguably undermines one of the pillars of the EU merger regime – the "*one-stop-shop*" principle obviating the need for multiple filings.

Illumina/Grail – a recent referral to the European Commission

Illumina/Grail[33] is the first case illustrating the European Commission's changed approach. Interestingly, this referral was not initiated by the Member States, but rather by the European Commission, which wrote to NCAs inviting them to refer the case.

Following unsuccessful attempts to challenge the decision before courts in France and the Netherlands, Illumina appealed to the General Court.[34] Illumina argued that the European Commission lacks jurisdiction to review mergers referred to it by NCAs that do not have jurisdiction under national rules because the mechanism was designed to cover countries with no national regime. The General Court rejected these arguments, commenting that the Article 22 referral procedure "*supplement[s]*" the EU merger control thresholds.[35]

Illumina also argued that the new approach to Article 22 was incompatible with the "*one-stop-shop*" principle and contrary to the EU legal principles of legal certainty, subsidiarity and proportionality. Again, the General Court rejected these grounds of appeal.

In addition, Illumina raised several procedural grounds of appeal. The most interesting relates to timelines. Illumina argued that the referral request had been submitted after the 15-working-day deadline set out in Article 22. Illumina argued that the 15-working-day period should run from the time the transaction was made public. The General Court held that "*made known*" requires the "*relevant information to be actively transmitted to that Member State*",[36] meaning that the 15-working-day period begins when the NCA is provided with the relevant information. This vague standard will make it more difficult for companies to self-assess and include appropriate clauses in transaction documents while giving considerable flexibility to authorities.

The European Commission has indicated that it is open to similar referrals in future and suggested that it had "*a few acquisitions within [its] sights that may be relevant candidates for Article 22. But that is not a given*".[37] However, Commissioner Vestager also indicated that it is "*not an open door for bringing in an indiscriminate number of new cases*" and "*should not be the cause of any uncertainty for market players*".[38] In practice, however, matters may be less clear cut, particularly pending Illumina and Grail's appeals.[39]

Practical considerations following *Illumina/Grail*

In light of the revised guidance regarding Article 22, merging parties may wish to consider proactively approaching the European Commission or NCAs where they anticipate the possibility of a referral.

Careful legal and economic analysis will be needed, including consideration of a number of factors such as: a comparison between the valuation of companies to revenues generated; the identification of recently awarded or patents in progress; market share growth or revenue growth, including market trajectories; and "*conglomerate effects*" in any overlapping, vertically integrated and "*related*" markets. In appropriate cases, acquirers will need to ensure that transaction documents reflect the risk of a referral request in the conditions precedent and, potentially, in relation to the long-stop date.

Where complex issues may arise, it is important to engage early and often with regulators, as well as maintaining consistent arguments as between jurisdictions.

Parallel investigations on both an EU and national level

Article 22 referrals raise the prospect of parallel investigations by the European Commission and EU NCAs. For example, in *Meta (formerly Facebook)/Kustomer*[40] the European Commission accepted a referral from the Austrian NCA (joined by a number of other EU Member States);[41] however, the *Bundeskartellamt* in Germany refused to join the referral request and opened its own proceedings.

Although major transactions are frequently subject to parallel merger reviews around the world, the *Meta/Kustomer* transaction highlights the potential for a combination of Brexit and Article 22 to increase the complexity of the review process even within Europe. The CMA had already completed its review and the European Commission's Phase 2 review was well under way before the *Bundeskartellamt* opened its Phase 1 review. The deal took approximately 16 months from announcement to final clearance.

The *Bundeskartellamt* primarily relied on the European Commission's findings about the customer relationship management ("**CRM**") segment. However, the *Bundeskartellamt* also looked at broader "*ecosystems*" created by social media that are supported by online advertising, and assessed whether Meta could use data gained through Kustomer to strengthen its position in this ecosystem. It also examined whether Meta could use Kustomer to cultivate relationships with end-users using Meta's online shops.[42] The significance of ecosystems is discussed under substantive theories of harm below.

In this case, the *Bundeskartellamt* reached the same conclusion as the European Commission. However, in future cases an NCA could deviate from the European Commission's findings, and the examination of additional markets by different authorities raises costs for companies.

Practical implications of parallel investigations

Technology companies need to brace themselves for potential diverging outcomes of multiple notifications that may have an impact on both the outcome of the review, as well as potential remedies.

As a practical matter, preliminary assessments will need to look at various plausible market definitions both when assessing risk and contemplating likely remedies. With regard to remedies, it is important to remember that authorities increasingly diverge on the weight that behavioural remedies carry compared to structural remedies. In particular, regulators in certain jurisdictions (such as the UK, Australia and Germany) increasingly prefer structural remedies to behavioural remedies, commenting in a joint statement that "*the increasing complexity of dynamic markets and the need to undertake forward-looking assessments require competition agencies to favour structural over behavioural remedies*",[43] while regulators in other jurisdictions (such as the European Commission) may be more receptive to proposed behavioural remedies. Notably, the *Bundeskartellamt* only accepts behavioural remedies in limited and fact-specific circumstances to the extent that they do not require ongoing monitoring by the competition authority or a third party.[44]

A proactive approach to timeline management will become increasingly important, especially where document requests are expected, and merging parties should take steps to actively attempt to align requests and submissions between various authorities.

Expansive application of the UK share of supply jurisdictional threshold

The CMA has flexibly used its existing tools to review transactions involving tech companies. The share of supply threshold, which permits the CMA to assess a merger where (as a result of the merger) a share of 25% or more in the supply or consumption of goods or services of any description in the UK (or a substantial part of it) is created or enhanced, is an inherently flexible tool. The share of supply test has enabled the UK regulator to review several transactions that the European Commission did not review (such as *Facebook/Instagram*[45] and *Google/Waze*[46]). In applying the share of supply test, the UK has shown considerable flexibility, relying not only on turnover-based market shares, but also other metrics such as the number of R&D employees engaged in a particular field of research.[47]

The CMA and the UK's Competition Appeal Tribunal ("**CAT**") have established a relatively low bar in terms of local nexus. In April 2020, the CMA blocked Sabre's acquisition of Farelogix, concluding that the merger would be expected to result in a substantial lessening of competition in IT solutions supplied to UK airlines to enable travel agents to make bookings. Sabre supplied these services through its global distribution system to UK airlines, whereas Farelogix supplied the services through its FLX Services to one UK airline (British Airways), in the context of its interline arrangement with American Airlines.

Sabre appealed to the CAT. Sabre argued that Farelogix did not supply the services in the UK, as British Airways received the services via an agreement with American Airlines. However, the CAT found that this was enough to show that Farelogix supplied services in the UK. Sabre also alleged that since Sabre's pre-merger share was already greater than 25%, the CMA should have had to show that the share of supply had increased post-merger. The CAT found no issues with the methodology applied by the CMA and noted that all that is needed is an increment of "*some real value*".[48] The CAT's judgment supports the CMA's broad discretion in applying the share of supply test and has naturally been welcomed by the CMA.[49]

Similarly, in *Meta/Kustomer* the CMA emphasised that the share of supply test is satisfied "*so long as [the] share is increased as a result of the merger, regardless of the size of the increment*".[50] The CMA also noted that the increment is likely to be small when a large company acquires a nascent or small competitor (as is the case in killer acquisitions) and referred to the CAT's judgment in *Sabre Corporation v Competition and Markets Authority*, noting that there is "*no de minimis threshold when assessing the increment*".

Acquisition of minority shareholdings

Another important point to note in relation to tech deals is that stake building may require merger control notifications to be made to NCAs.

For example, in *Amazon/Deliveroo*[51] the CMA approved Amazon's acquisition of a 16% minority stake in Deliveroo after a Phase 2 review, over 13 months after the interim enforcement order in June 2019. The CMA held that the transaction could harm competition by discouraging Amazon from re-entering the online restaurant food market or further developing its presence in the online convenience grocery delivery market in the UK.[52]

The acquisition of "*material influence*" confers jurisdiction on the CMA. The CMA's guidance indicates that an acquisition of a stake of 15% or more is liable to be examined to see whether the holder can influence the policy of the company concerned (although shareholdings below 15% can also give rise to material influence).[53]

Material influence is assessed on a case-by-case basis. In *Amazon/Deliveroo*, the CMA considered various factors, including Amazon's expertise in areas such as the operation of online marketplaces, logistics networks and subscription services, which would allegedly allow Amazon to influence Deliveroo's shareholders and board members. The CMA acknowledged that some of Deliveroo's shareholders are experienced and sophisticated investors with current or past shareholdings in other food or technology companies but found that Amazon benefits from deeper knowledge and expertise of the markets in which Deliveroo operates.

Practical considerations in UK mergers

The decision in *Sabre/Farelogix*[54] emphasises the CMA's flexibility to assert jurisdiction and highlights the need to consider engaging with the CMA (e.g. by submitting a briefing paper to the Mergers Intelligence Committee) early on in a transaction.

Private equity investors, as well as trade buyers, will also need to be mindful that stake building – even if it only relates to minority interests – can trigger a long and detailed merger review. The CMA's broad discretion in applying the share of supply test in assessing jurisdiction may give rise to complex issues, particularly where the ultimate beneficiary controls multiple funds and there are cross-shareholdings.

Substantive Issues: Market Definition

Market definition is a standard framework for assessing the competitive effects of a merger. Competition authorities have

traditionally applied the so-called small but significant non-transitory increase in price ("**SSNIP**") test to assist with defining the scope of the relevant market. However, there are particular difficulties in applying this test to digital markets, especially where no monetary price is charged for a given service. Broad notions of "*price*" are emerging, with a case pending before the CAT in the UK where the applicant has alleged that users of Meta's social networking services have paid an "*unfair price*" by providing their personal data.[55] It remains to be seen whether regulators and the courts will be receptive to the concept of personal data as a price in the context of "*free*" services.

These challenges are particularly acute for transactions involving platforms, which are often described as being multi-sided markets because they facilitate interactions between multiple different user groups (for example, merchants, consumers and advisers). While regulators have considered issues relating to multi-sided markets for many years (for example, in relation to media mergers[56]), there are differentiating factors in the digital space, particularly the size, breadth and geographic reach of some platforms.

This challenge has been acknowledged by the CMA in its merger guidelines,[57] where it notes that it may be difficult to conduct a hypothetical monopolist test in multi-sided markets because: (i) there is no (or possibly no) single price to which to apply a SSNIP test; (ii) the effect of a SSNIP on the demand of one set of customers may be exacerbated by indirect network effects; and (iii) the constraints on the merging parties' products may come not only from other two-sided intermediaries but also from "*one-sided*" firms serving one set of customers. However, the guidelines do not suggest an alternative approach.

The fact that prices are zero on one side of the market (e.g. to viewers, readers or users) does not mean that this feature should be excluded from the market definition and competitive assessment. If the traditional SSNIP test is not considered appropriate, a possible option is an adapted version of the SSNIP test focused on quality degradation or improvement.[58] Quality is not as straightforward to measure, as it often covers a number of different dimensions of a product or service and is likely to be interpreted differently by different users.

In the behavioural context, in the *Google Android* case,[59] the General Court upheld the European Commission's new test: whether users would switch as a result of a small but significant non-transitory decrease in the quality (the "**SSNDQ test**") of the operating system.[60] Noting that the test had not previously been used by the European Commission, the General Court stated that it can be a useful tool when analysing zero-price markets because competition can take place in relation to price but also quality and innovation. The General Court also confirmed that the SSNDQ test does not require "*a precise standard of degradation to be set beforehand. All that matters is that the quality degradation remains small, albeit significant and non-transitory*".[61] As mentioned, the SSNDQ test had not previously been used by the European Commission; however, now that it has been affirmed by the General Court, it may be applied in future merger cases where the SSNIP test is less relevant or harder to apply.

Practical points to consider when assessing market definition

Given the challenges in defining digital markets, some competition authorities have begun to place less emphasis on defining the precise scope of the market. This approach involves increased scrutiny of internal documents – a trend long enforced in the US and increasingly relevant in other jurisdictions. As a practical matter, companies and advisors will increasingly need to review pre-existing internal documents at an early stage of a deal risk assessment and to conduct a thorough qualitative as well as quantitative assessment.

Substantive Issues: Theories of Harm

As markets evolve, so do the theories of harm applied by competition authorities. In this section, we focus on four theories of harm increasingly raised in transactions in tech: (i) killer acquisitions; (ii) network effects and access to data; (iii) creation of larger ecosystems of complementary services; and (iv) competition in innovation.

Killer acquisitions

Competition authorities have repeatedly raised concerns about so-called killer acquisitions in the digital sector, with some stating that "*these acquisitions, over time, represent a potentially enormous loss of consumer welfare*".[62]

As mentioned above, this is one of the concerns that prompted the European Commission to update its guidance on Article 22. Killer acquisitions have also been discussed in the development of the DMA, with the requirement for gatekeepers to notify the European Commission of all mergers involving another platform provider from the digital sector, designed to ensure that the European Commission is more easily able to monitor the market and identify any possible killer acquisitions at an early stage.

Some argue that digital platform markets, in particular, are prone to tipping and are characterised by significant network effects and innovation. Competition authorities may consider whether a large incumbent acquiring a small, innovative start-up firm may adversely affect competition by removing a potential competitor that could have grown rapidly to compete with the incumbent. In the summary of its Phase 1 decision to refer Microsoft's acquisition of Activision for a Phase 2 review, the CMA commented that "*by leveraging ABK's content and Microsoft's wider ecosystem, Microsoft will have an unparalleled advantage over current and potential cloud gaming service providers. This could result in… the market 'tipping' to Microsoft, and ultimately deny consumers the benefits of competition between new and emerging providers*".[63] Examples of recent transactions where this has been considered include *Amazon/Deliveroo*,[64] *JustEat/Takeaway*[65] and *Meta/GIPHY*.[66]

In such cases, authorities may consider that the future competitive constraint provided by the start-up on the incumbent may be significantly greater than the start-up's current market position suggests. This raises an important question about the relevant counterfactual for the merger assessment, which involves trying to predict: (i) how big the start-up would have become in the absence of the merger; and (ii) how the other players in the market would have behaved. Importantly, this analysis must include consideration of how other players (and any new potential entrants) would develop. Otherwise, there is a risk that the assessment will include a confirmation bias that only considers the growth of the target/merged entity and will fail to account for the growth potential of other rivals.

Authorities will likely pay particular attention to dynamic competition in digital sectors. According to the CMA, "*dynamic competition is what leads firms to innovate, through a process of creating new, better products for consumers over time*".[67] In its appeal to the CAT, Meta unsuccessfully challenged the CMA's conclusion that its acquisition of GIPHY would have "*substantially reduced dynamic competition*".[68] Agreeing with the CMA, the CAT commented that, in relation to dynamic competition:[69]

(a) It is unhelpful to distinguish between the current position and future market trajectory as the facts that "*render competition dynamic will likely be present in the market*" but may not have "*manifested themselves*".

(b) Traditional analytical tools (such as "*market share, market definition, etc*") are "*less likely to be determinative*".

(c) Identifying criteria for assessing whether dynamic competition exists "*is extremely difficult*". In *obiter* comments, the CAT commented that assessing dynamic competition "*involves a far greater consideration of innovation and invention – in short, potentiality – rather than analysis of an existing market or an assessment of the future trends that lie within it*".[70]

Naturally, all these approaches exacerbate the uncertainty in the forward-looking analysis that is inherent in merger control.

As evidenced by the introduction of transaction value thresholds, regulators increasingly focus on the valuation of the target business. Regulators are concerned that a buyer's high valuation of a company generating little or no revenue indicates the level of benefit that the buyer expects to achieve from the transaction because, for example, it will remove a potentially important future rival. Examples of deals that have drawn attention in relation to deal value include: Facebook's USD 19 billion acquisition of WhatsApp in 2014, Microsoft's USD 26.2 billion acquisition of LinkedIn in 2016, Google's acquisition of Motorola Mobility for USD 12.5 billion in 2011 and Illumina's acquisition of Grail for USD 8 billion in 2020.

The European Commission acknowledges that "*the chance for start-ups to be acquired by larger companies is an important element of venture capital markets: it is among the main exit routes for investors and it provides an incentive for the private financing of high-risk innovation*".[71] Thus, regulators need to tread carefully to avoid over-enforcement and companies need to be careful in presenting and preparing their deal rationale to make clear that it is pro-competitive and ensure that the reasons underlying valuations are carefully documented.

Complementary services, network effects and access to data

Merging tech companies should also take into account possible "*conglomerate effects*" in their risk assessment.[72] Conglomerate mergers, which do not involve the removal of a direct competitor, provide substantial scope for efficiencies and synergies and are typically less likely to raise concerns. However, in certain segments this may not be the case. Theories of harm may focus on the possible foreclosure of rivals who may be hampered in their access to markets and potentially to supplies (e.g. as a result of tying or bundling products or services within a platform's overall ecosystem).

For example, in *Meta/Kustomer*, the European Commission was concerned that Meta would have the ability and incentive to foreclose Kustomer's rivals and new entrants by denying or degrading access to the application programming interfaces ("**APIs**") for Meta's messaging channels. To address these concerns, Meta offered access commitments covering: (i) its publicly available APIs for its messaging channels to competing CRM software providers and new entrants; and (ii) if any features or functionalities of Meta's messaging services are improved or updated, Meta has committed to make equivalent improvements available to Kustomer's rivals and new entrants. The commitments will last for 10 years.

Conglomerate theories of harm were also raised in *Microsoft/LinkedIn* and *Microsoft/Skype*.[73] The European Commission considered whether post-merger Microsoft could have profitably tied LinkedIn and/or Skype with other Microsoft products, thereby foreclosing alternative providers of these services. In *Microsoft/LinkedIn*, the European Commission considered that network effects could tip the market in LinkedIn's favour. To address the European Commission's concerns, the parties offered commitments to: (i) ensure that PC manufacturers would be free not to install LinkedIn on Windows and enable users to remove LinkedIn if it was pre-installed; and (ii) grant access to all Office APIs to third parties (i.e. an access remedy). Conversely, in *Microsoft/Skype*, the European Commission considered that the tendency of users to multihome limited the benefits that tying would have delivered, as consumers did not simply use whatever communication service was provided with Windows, and pre-installation did not prevent alternative providers of communication software from competing.

Complementary services

The Lear report[74] found that acquisitions often target "*companies spanning a wide range of economic sectors and whose products and services are often complementary to those supplied by the acquirers*". This highlights the complexity of the business models pursued by digital companies, which creates challenges from a merger control perspective.

However, recent decisions show how parties may be able to resolve initial concerns based on conglomerate effects in such cases. The CMA's decision in *PayPal/iZettle*[75] illustrates the importance of considering possibly complementary offerings as well as traditional competitors – PayPal's online payment service solutions and iZettle's in-store/offline product were assessed in the context of a possible "*multi-channel solution*".[76] Although the counterfactual considered by the CMA showed that PayPal would likely emerge as a stronger player, the CMA did not identify competition concerns due to sufficient competitive constraints on PayPal from traditional payment providers and other offline payment services. The CMA found that the elimination of iZettle as nascent competitor in the multi-channel space did not raise competition concerns, as iZettle would only have been able to develop its offering slowly and would have remained a marginal player for the foreseeable future. The CMA also found that other significant competitors would be more significant constraints on PayPal.

Network effects and access to data

Preliminary assessments of deals must consider not only shares based on turnover, but also whether authorities may see the accumulation of data as giving rise to a substantial lessening of, or impediment to, competition. Demonstrating that a dataset is not unique and is obtainable from multiple sources may be one way for parties to address the theory of harm adopted by the European Commission in *Microsoft/LinkedIn*.[77] The European Commission assessed whether the combination of the parties' data could strengthen the merged entity's position in online advertising and whether the combination of two previously independent datasets had the potential to increase the merged entity's market power in respect of the supply of this data, increase barriers to entry/expansion in the market for online advertising, or simply remove the pre-merger competitive constraint that the parties were exerting on each other (based on the data they controlled). This theory of harm was dismissed, mainly based on the evidence that a large amount of data that was valuable for advertising purposes was still available and not in the exclusive control of the merged entity.

In *Meta/Kustomer*, the European Commission and the CMA also considered, at Phase 1, whether the transaction would enable Meta to obtain data more easily from businesses using Kustomer's CRM software, which would increase the data available to Meta for targeted digital advertising. However, both concluded that the additional data would not raise barriers to entry due to Kustomer's small size and the availability of similar data for rivals.

In the CMA's review of Meta's acquisition of GIPHY,[78] concerns were raised that Meta could change the terms of access to require TikTok, Twitter and Snapchat, for example, to provide more user data to access GIPHY GIFs. Consumer data is valuable to advertisers because it enables them to better target

audiences. The proposed open-access remedy, which included (among other things) an obligation not to use data obtained through the GIPHY APIs for Facebook's advertising business, was rejected by the CMA. The CMA thought that a behavioural remedy would not eliminate a substantial lessening of competition and that a complete divestiture would be necessary, feasible and proportionate. Interestingly, the CMA considered Facebook's argument that a five-year remedy would be at the "*outer edges of what could be considered under a dynamic loss of competition theory*".[79] However, the dynamic nature of the market meant that there was some uncertainty about whether the competition concerns will endure beyond the five-year period. The CMA also noted that Facebook had not adduced any evidence to demonstrate that any competition concerns would have been addressed by the end of the five-year period. This suggests that the CMA may be willing to consider behavioural remedies even if it did not consider this case to be a suitable one and that duration is likely to be an important negotiation point in future (as is often the case in behavioural remedies in various sectors).

The CMA required the transaction to be unwound. Its approach contrasts with that of the European Commission in *Google/Fitbit*, where a data silo commitment, under which Google would segregate data collected by Fitbit's wearable devices from other data used for advertising, was accepted.

Practical considerations in conglomerate mergers

Merging tech companies can expect rigorous examination of all markets, including so-called neighbouring or related markets. Competition authorities are likely to consider patterns of acquisitions even in relation to products not related to the merger. More emphasis will be placed on assessing data as a critical input that can support network effects and create barriers to entry. Cases have shown that competition authorities can adopt a very broad approach when assessing competition concerns, which includes the assessment of data bundles across ecosystems. As mentioned before, tech companies also need to prepare for a more rigorous review of internal documents.

Loss of competition in innovation

Innovation-based theories of harm in non-digital mergers

Innovation is emerging as one of the criteria by which regulators will assess the likely effects of a merger.[80]

In *Medtronic/Covidien*,[81] the merging parties were active in the medical devices sector, and Medtronic was considered the market leader. The European Commission noted that the target (Covidien) was developing its own device, Stellarex, and there were few other competitors in the market. The European Commission raised concerns that the merger would remove a future competitor to Medtronic and the merged entity would have the incentive to discontinue the development of Covidien's pipeline product, depriving the market of an important innovation. To address these concerns, Medtronic committed to sell Covidien's Stellarex business, with all the assets necessary to bring the innovation to market.

Dow/DuPont[82] illustrates how authorities may review the merging parties' incentives to innovate post-merger. The European Commission found that the parties competed as vertically integrated developers and manufacturers of pesticides, with innovation being considered of particular importance in the crop-protection industry. The European Commission's concern was that the merger threatened competition in innovation by:

(a) removing the parties' incentives to pursue ongoing parallel innovation efforts, and incentivising the parties to discontinue some of their pipeline products; and

(b) removing the parties' incentives to innovate in new pesticides (i.e. the merged entity's incentive to innovate was considered lower than the sum of the parties' incentives in isolation).

Due to concerns in relation to innovation competition, the European Commission required the divestment of DuPont's global pesticides business, including its R&D division. Concerns of this type are likely to be increasingly relevant to the tech sector. However, given the potential sensitivity of this type of information from a competition law perspective, judicious use of outside counsel and confidentiality arrangements will be essential to balancing compliance and deal risk management.

Innovation-based theories of harm in the digital space

Given the highly innovative nature of digital markets, regulators may also advance concerns about the possible impact of the merger on innovation (e.g. as a result of the combination of two important innovators, or a merger that results in the elimination of a firm with a promising pipeline of products).

The European Commission considered the impact on competition in innovation in *Google/Fitbit*[83] but concluded that there was no market where Fitbit was the only or main source of pressure on Google to innovate and thus did not consider the theory of harm in detail. The European Commission also stated that it would examine whether the proposed acquisition of Arm Limited by NVIDIA would lead to reduced innovation in semiconductors because: (i) Arm's licensees might be reluctant to continue sharing commercially sensitive information with the merged entity because they compete with NVIDIA; or (ii) NVIDIA may choose to refocus Arm's R&D spending on products that are most profitable for NVIDIA downstream, to the detriment of players heavily relying on certain Arm intellectual property ("**IP**") in other areas.[84] In February 2022, the parties announced that the transaction had been aborted due to "*significant regulatory challenges*".[85]

The relationship between market concentration and innovation is complex. Competition in innovation can take place over a long period, and results are unpredictable. In certain segments, higher concentration may arguably lead to greater innovation because firms are incentivised to incur R&D spending as a result of the pay-off of innovation.

Practical considerations in innovation-intensive mergers

It is hard to assess how a transaction will affect innovation. Using R&D spending as a proxy for innovation is difficult and potentially inaccurate because synergies of combining research teams and knowledge can result in lower R&D spending but increased innovation. Money may be redirected to new areas of research and innovation, thereby resulting in increased benefits for consumers. There is also an inherent tension between using R&D as a parameter of innovation and the notion of supposed killer acquisitions, where small companies with limited capacity for R&D spend can be seen as significant competitive constraints.

Proliferation of FDI Regimes

In recent years, there has been a proliferation of FDI regimes worldwide. In March 2019, the EU enacted the EU Screening Regulation,[86] which contains a cooperation mechanism for screening FDI in EU Member States. The cooperation mechanism enables EU Member States and the European Commission to exchange information, provide comments and issue opinions on investments made by foreign entities and nationals.

In March 2020, the European Commission encouraged Member States without a (fully fledged) screening mechanism to set up such a mechanism and, in the meantime, to use all other available options to address cases where FDI would create a risk to security or public order in the EU. As of September

2022, 25 of 27 Member States either had FDI screening mechanisms or had a consultative or legislative process to adopt such a mechanism under way.[87] Belgium, Ireland and the Netherlands are three of the most recent Member States to propose new or expanded FDI screening regimes.

Many of these FDI regimes (both in Europe and elsewhere) capture investments in certain technologies; for example, advanced robotics, artificial intelligence, computing hardware, data infrastructure, military and dual-use, quantum technologies, and satellite and space technologies.

Increased scrutiny of tech deals

As with merger control, there is an increasing concern about transactions relating to technology, particularly where technology could be used in the defence/military sector. Typically, the thresholds for triggering notification under an FDI regime are lower than merger control thresholds. This will result in a greater number of tech mergers being scrutinised by a regulatory body. Notably, the two prohibitions to date in the UK related to investments in dual-use technologies:

(a) On 20 July 2022, the Secretary of State for Business, Energy & Industrial Strategy in the UK ("**SoS**") prohibited a licence agreement, which would have permitted a Chinese technology company (Beijing Infinite Vision Technology Company Ltd) to use IP relating to certain vision-sensing technology (SCAMP-5 and SCAMP-7) to develop, test and verify, manufacture, use and sell licensed products developed by the University of Manchester. The SCAMP technology has been described by the University of Manchester as a cutting-edge approach that allows the pixilation of data to happen in a faster and more efficient way on a sensor chip.

(b) On 17 August 2022, the SoS blocked the proposed takeover of Pulsic, a UK technology company, by Super Orange HK. Pulsic is an electronic design automation company, which develops software used to build electrical circuits. The products could potentially be exploited to build defence or technological capabilities. The proposed acquirer (Super Orange HK) is based in Hong Kong but is reportedly controlled by a Shanghai-based entity that has Chinese State backing.

Practical considerations of FDI scrutiny

FDI regimes can also involve long reviews, which may be less predictable than merger control review and thus impact merger timelines more substantially.

Often, merger control and FDI reviews will take place in parallel and information can be exchanged between the authorities. Parties will need to consider their conditions precedent carefully to ensure that clearances under both regimes are included in relevant deal documents and that sufficient time is built into the transaction timetable, including the risk of diverging remedies or conclusions by the different regulators. Likewise, it is important to coordinate interactions with authorities between counsel responsible for FDI and competition reviews.

Conclusion

The digital sector continues to attract scrutiny from regulators around the world. While regulators have recognised the importance and benefits of digital markets for consumers, perceived under-enforcement of mergers in digital markets has resulted in a desire to demonstrate a "*tough stance*" on digital mergers, demonstrated by a number of high-profile deals being blocked or aborted due to regulatory scrutiny in the last few years.

As we move away from a world in which simple comparisons to the lawyers' fictional concept of products, known as "*widgets*", can be made to assess traditional parameters of competition, regulators have responded by introducing legislative reforms and new merger thresholds that are designed to capture the nature of digital markets. Regulators are also proactively monitoring for transactions that may affect competition and are making use of referral and powers to call in transactions for review. This inevitably increases uncertainty for companies involved in M&A activity, thus early engagement with advisors (and potentially regulators) will be of paramount importance.

Regulators must strike the right balance in adopting a proportionate approach to merger enforcement, avoiding any chilling effect on innovation. The risk of unintended consequences is particularly acute given the fast-moving and dynamic nature of digital markets characterised by high levels of innovation. Proactive engagement with regulators to explain the transaction rationale and pro-competitive effects of a particular transaction may help to mitigate this risk.

In summary, digital companies need to seek advice at the earliest possible stage of a deal. Merger analysis will involve a complex legal analysis, including robust economic modelling looking at various, properly defined markets, and determining whether (new) thresholds have been met. Deals that do not meet thresholds can still be called in for review. Even where remedies are accepted, different competition authorities may reach different outcomes in relation to the adequacy of remedies. Competition authorities may also favour structural remedies instead of behavioural remedies, particularly if it is difficult to determine their adequacy in a quickly evolving dynamic market. Technology also falls under a sensitive area for FDI regimes warranting additional filings from a regulatory perspective. Beyond deals, digital companies should pay attention to internal documentation on a day-to-day basis given that regulators are increasingly relying on internal documents to understand the markets in which they operate.

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22. The Austrian Competition Authority will typically find that there is no sufficient domestic activity if the turnover of domestic target companies is below EUR 1 million, provided that this turnover adequately reflects the market position and the competitive potential of the target company. In addition, a share of >10% on a competitive relevant segment in Austria is to be considered significant domestic activity according to Austrian case law.
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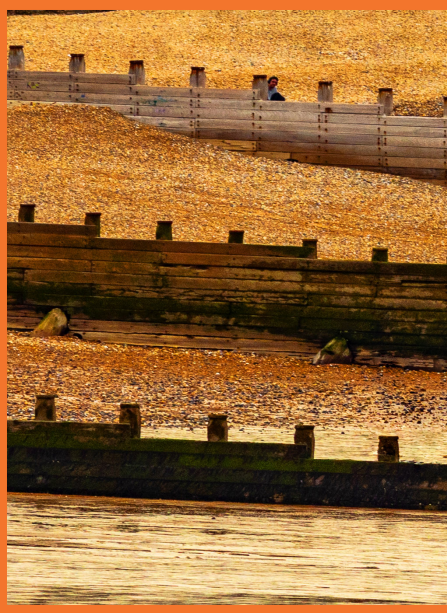

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