Assessing the Efficiency Claim in European Merger Policy

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Executive Summary

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Extended Abstract

In competition policy Mergers and Antitrust are two highly related areas in the field in law enforcement. In both areas the competition authority–either European or national–faces a severe informational restraint but these restraints differ in their quality due to the role of competition policy in these areas. In this paper I contrast the problems of law enforcement in the areas of antitrust and merger policy. In particular, I focus on the information available and necessary in order to investigate anticompetitive practices or proposed mergers. While information problems are eminent in both areas, in merger investigations they prevail in the forecasts on firms' future behavior and consumers future benefit and in antitrust investigations they prevail when retracing firms' past behavior.

Antitrust aims at inhibiting abusive conduct of dominant firms that is detrimental to consumers. In order to start an investigation the competition authority needs to have an initial reason for distrust. These can be complaints by competitors or consumers (or consumer associations). Any investigation will rely on data that the Commission obtains from the firms active on the market. Lately DG Competition has conducted an investigation on the energy sector.[1] Certainly, the willingness to cooperate of firms which are suspected to anticompetitive practices is limited. While some data like prices, quantities and contracts contain precise information, cost data are–at least to a certain extent–subject to the firms' discretion. Firms anticipating the investigation by regulators may behave strategically. This renders the Commission's work more difficult.

The modern economic approach of the Commission envisages to employ quantitative methods in their investigation. Recently developed methods allow to infer more information from observable data than before. Examples are Berry (1994), Berry, Levinsohn and Pakes (1995), Nevo (2000), Petrin (2002) or Verboven (2002). Their use in legal procedures are subject matter of the ongoing discussion on the 'more economic approach' in competition policy.

Merger Policy also involves detailed investigations by the Commission. However, these investigations are initiated by a precise notification. Here the informational problem prevails in the assessment of the efficiency claims that were introduced in the recent review of the Merger Regulation.[2] By this feature merg-

[1] http://europa.eu.int/comm/competition/antitrust/others/sector_inquiries/energy/ See the 'Energy Sector Inquiry–Issues Paper' pursuant to Article 17 of Regulation 1/2003 EC. They intend to deepen this investigation in the Tender COMP/2005/B-1/010 where an extensive quantitative analysis of the collected data is to be conducted.

[2] Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings No C31, 5.2.2004, p. 3 OJ L 31, 5.2.2004

ing firms my claim that the proposed merger contributes to social benefit by an increased benefit. This can refer to cost reduction in production or distribution, R&D and innovation which may result in the introduction of new products.

Although there have been only a minor number of cases that have been forbidden by the Commission (18 cases by mid of 2004) a significant number of mergers were permitted subject to some obligations (171 cases by mid of 2004).[3] A detailed analysis by the DG Competition, the *Merger Remedies Study*, has been published in October 2005.

The efficiency gains that are claimed by the merging parties have to be assessed by the Commission. Certainly, this entails to some extent discretionary analysis. In this aspect the assessment of mergers and a potential anticompetitive practice are very similar. Both rely on estimations of future market outcomes or contrafactual market outcomes, respectively. In this paper we propose a classification for the assessment of the efficiency claim. This will entail the notion of a 'credible efficiency claim':

1. Increased consumer benefit immediately raises the profit of the merging parties.

2. Increased consumer benefit comes along with the merging parties' profit maximizing behavior.

3. Consumers benefit from a merger only if additional obligations or conditions are imposed.

4. Consumer benefit only, if the merging firms perform some additional effort.

For (1) and (2) the enforcement poses no problem because the firms' interest coincides with the Commissions' objectives. (3) includes a remedy that can be enforced. Efficiency claims in category (4) rely on the goodwill of the merging firms. These are to be identified in the assessment of the merger proposal. Either they are taken into consideration in the evaluation–then the Commission should employ mechanisms that help enforcing these claims–or they are to be disregarded.

This paper is a part of a research project on the economic and empirical foundations of innovative performance following market concentration. It aims at finding applicable rules to detect and prevent anti-innovative behavior in merger notifications.

[3]These numbers were published in a Communication from the Commission: A pro-active Competition-Policy for a Competitive Europe, COM(2004) 293 final, 20.4.2004.

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