



**BUNDESKARTELLAMT**

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## **Conglomerate Mergers in Merger Control**

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## **Review and Prospects**

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**- Discussion paper -**

**Bundeskartellamt**

**Discussion paper**

for the meeting of the Working Group on Competition Law  
on 21 September 2006

Conglomerate Mergers in Merger Control

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Review and Prospects

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## A. Introduction

Decisions on conglomerate mergers are taken within a borderline area of merger control which places great demands on competition analysis. The difference between conglomerate mergers and horizontal mergers is that no actual competitor is eliminated. As a result conglomerate mergers only create anticompetitive effects under certain conditions. Hardly any other area of competition law is as controversial among competition economists and competition law experts as the practice applied to conglomerate mergers. The views on this are also very diverse among the competition authorities.<sup>1</sup> This was particularly apparent from the differing assessments of the planned GE / Honeywell merger by the Commission and US Department of Justice. Whereas the International Competition Network (ICN) was able to agree on common principles of interpretation in other areas of merger control a few months ago, differing views persist on conglomerate mergers.<sup>2</sup> Discussion on this has been further fuelled by recent decisions. Both the ruling of the Court of First Instance (CFI) in the GE / Honeywell case as well as the Bundeskartellamt decision in the Axel Springer / ProSiebenSat.1 case have met with great response among the professional public.<sup>3</sup> Furthermore, the Commission is in the process of drafting its future principles of interpretation for non-horizontal mergers, the publication of which is expected at the end of this year.

This paper is meant as a contribution to this discussion. It deals firstly with the development of competition law practice as applied by the competition authorities in the USA, EU and Germany. Here differences can be established both over time as well as between the various jurisdictions. The second part of the paper reappraises and summarizes the current state of economic theory providing at the same time a potential framework for the analysis of conglomerate mergers. Finally, it summarizes some key propositions for assessing conglomerate mergers in future.

In this paper, under the term "conglomerate mergers" those mergers are defined in which there are no horizontal overlaps or vertical relationships between the parties to

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<sup>1</sup> For an account of the positions of 14 competition authorities refer to OECD (2002).

<sup>2</sup> Cf. ICN (2006).

<sup>3</sup> Cf. e.g. Bohne (2006), Bonin (2006), Drauz and König (2006), Gounalakis and Zagouras (2006), Kuchinke and Schubert (2006), Pflanz (2006), Säcker (2006).

the merger in the relevant product markets.<sup>4</sup> However, complementary or substitutional relationships may exist between the products of the merging undertakings. The products are to a certain degree complementary if the benefit to the customer is greater from the combined consumption than it would be from separate consumption. A certain substitutional relationship exists if the products are interchangeable for certain customers or areas of use. Both features do not exclude one another and can therefore exist simultaneously.

## **B. Assessment of Conglomerate Mergers in Practice**

### **1. The practice in the USA**

#### *Restrictive Practice in the 1960s and 1970s*

In 1950 Section 7 of the Clayton Act (15 U.S.C. § 18) was amended by the Celler-Kefauver Act by which a merger is now considered illegal if it is likely to lead to a substantial lessening of competition (the so-called SLC Test). The express aim of the legislator was to improve the way in which conglomerate mergers are covered.<sup>5</sup>

Following the amendment to the law the US competition authorities pursued a relatively restrictive practice in merger control both as far as horizontal and vertical mergers as well as conglomerate mergers are concerned. At the same time not only merger activity but above all the ratio of conglomerate mergers rose in the 1960s and 1970s.<sup>6</sup> The courts followed the practice of the competition authorities and prohibited a number of conglomerate mergers. The prohibitions and consent decrees<sup>7</sup> were based on different theories of harm which can be condensed into four groups<sup>8</sup> which do not preclude one another: the “Entrenchment Doctrine”<sup>9</sup>, the Elimination of Potential Competition, the Reciprocity Argument and the Increase of Aggregate Concentration.

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<sup>4</sup> According to this definition mergers between companies active in the same product market but different geographic markets do not fall under the category of conglomerate mergers.

<sup>5</sup> Cf. Dreher (1987), page 28.

<sup>6</sup> Cf. published by the US FTC in, among others, Möschel (1980), p. 206 ff.

<sup>7</sup> Consent decrees are the analogue to clearances subject to obligations/conditions.

<sup>8</sup> This group division is dealt with differently by various authors, cf. e.g. Bork (1978), p. 246 ff., Büscher (1983), p. 157 ff., Dreher (1987), p. 29 ff., Möschel (1980), p. 216 ff., Sullivan (1977), p. 631 ff.

<sup>9</sup> The doctrine was imprecisely defined and is based on market foreclosure effects, deterrence effects and efficiency effects.

“Entrenchment” was the most important theory of harm, by which anticompetitive effects can occur due to an increase in economic power, particularly in terms of financial power and its consolidation by the use of brand names. Firstly, the other competitors would reduce their competitive activities since they would fear cut prices or other retaliatory measures by the dominant company as a result of the increase in resources. As such expectations would dissuade other companies from entering the market, such increase in potential acted as an additional barrier to market entry. A leading case for the entrenchment doctrine is the Procter&Gamble / Clorox case. In 1957 Procter&Gamble, a manufacturer of many household products with the largest advertising budget in the USA at the time, acquired Clorox, the dominant company in the manufacture of household bleach products. In 1967 the Supreme Court ruled that Procter&Gamble’s large advertising budget, in particular, led to corresponding deterrent effects in the market for household bleach products.<sup>10</sup>

According to the second theory of harm anticompetitive effects can occur as a result of diminishing potential competition. The theory has two variants. One is that the “actual potential” competition would be reduced if the acquirer could have entered the market in a manner less harmful to competition (e.g. by acquiring a smaller competitor or by its own investments). The “perceived potential” competition would be reduced if the acquirer was previously perceived by the established competitors as a potential competitor and had thus limited the scope of action.<sup>11</sup>

According to the third theory of harm a conglomerate merger can create anticompetitive effects through reciprocity dealings. Accordingly, both parties to the merger could induce their customers or suppliers to transact future business with the respective other merging partner. Such tying practices could create market foreclosure effects in a similar way as vertical mergers. The leading case here is Consolidated Foods / Gentry. In this case the food company Consolidated Foods in 1951 acquired the second largest manufacturer of onion and garlic powder, Gentry. Consolidated Foods requested its suppliers, with some success, to purchase Gentry products. In 1965 the Supreme Court decided that this case also satisfied the

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<sup>10</sup> Cf. FTC v. Procter&Gamble Co., 386 U.S. 568 (1967). The Supreme Court quashed the judgement of the appellate court and rejected the case with the requirement that the merger be prohibited/dissolved.

<sup>11</sup> Cf. U.S. v. El Paso Natural Gas Co., 376 U.S. 651 (1964) and U.S. v. Falstaff Brewing Corp., 410 U.S. 526 (1973). Both cases involved companies which were active in the same product but different geographic markets and cannot therefore be classified as conglomerate mergers according to the definition made in this paper.

prohibition criterion because of Gentry's significant market share and the high probability of reciprocity dealings.<sup>12</sup>

According to the fourth theory of harm the anticompetitive effect already lies in the increase of the aggregate concentration. According to this approach it is not necessary to prove effects on individual markets defined as separate markets under competition law. Rather, the increase of aggregate concentration in itself should fulfil the prohibition criterion. As this argumentation was used only temporarily by the US Department of Justice's Antitrust Division in some of its consent decrees and in proceedings before the district courts, this was not substantiated by further clarification by the Supreme Court. Legislation proposals from 1979 directed against aggregate concentration did not receive a parliamentary majority.

### *Liberal practice since the 1980s*

Various reasons led to a complete reversal in US practice. From the early 1970s court proceedings against conglomerate mergers became increasingly unsuccessful.<sup>13</sup> The rather restrictive line adopted by the Supreme Court gradually changed. Courts of lower instance also increasingly began to set higher demands on the proof of anticompetitive effects in the case of conglomerate mergers.<sup>14</sup>

At the same time the line of argumentation of the liberal Chicago School gained prevalence in discussion among academia in the USA and within the US government. Its advocates also criticized, in particular, the practice of the courts and the competition authorities of acting against conglomerate mergers. Of particular influence in this respect were papers by Bork (1978) and Areeda and Turner (1980).<sup>15</sup> After the Reagan Administration came to power the heads of both US competition authorities were replaced with William F. Baxter and James C. Miller, both of which were attributed to the Chicago School.<sup>16</sup>

With the 1982 Merger Guidelines of the US Department of Justice the theories of harm based on entrenchment, reciprocity dealings and increase in aggregate

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<sup>12</sup> Cf. *FTC v. Consolidated Foods Corp.*, 380 U.S. 592 (1965). The Supreme Court quashed the judgement of the appellate court.

<sup>13</sup> According to statistics provided by Dreher the success rate of plaintiffs between 1964 and 1974 lay at 11 of 21 cases, between 1974 and 1984 only 5 of 31 cases. Cf. Dreher (1987), p.37.

<sup>14</sup> Cf. Dreher (1987), p. 29 ff.

<sup>15</sup> Cf. OECD (2002), p. 216.

<sup>16</sup> Cf. Möschel (1984), p. 560.

concentration were finally abandoned. In the Non-Horizontal Merger Guidelines which are still in force the elimination of potential competition therefore remains the only possible basis for intervention by the competition authorities.<sup>17</sup> Since then there have been no known cases in US practice of conglomerate mergers being prohibited. The closest that judgements came to prohibition were a number of consent decrees in merger proceedings not involving conglomerate mergers in which the US authorities have imposed behavioural remedies against possible tying and bundling practices.<sup>18</sup>

In connection with the GE/Honeywell case the US competition authorities have made clear their current position on the control of conglomerate mergers.<sup>19</sup> In their view competition authorities should only act against conglomerate mergers if they cause the elimination of potential competition.<sup>20</sup> On the one hand conglomerate mergers offered significant efficiency potential. On the other, possible anticompetitive effects could only arise under a number of conditions whose verification was determined by speculative predictions on the future behaviour of the market participants. The self-healing powers of the markets meant that no anticompetitive effects were to be expected in the long term or at least could not be predicted with sufficient certainty.<sup>21</sup> Erroneous prohibitions by the competition authorities and courts under these circumstances were therefore probable. Furthermore, ex-post instruments of abuse control, in particular claims for damages and fines, were effective deterrent mechanisms against possible abusive behaviour. Therefore ex-ante measures such as prohibition or clearance subject to conditions under merger control were unnecessary and involved the risk of preventing the efficiencies of conglomerate mergers.

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<sup>17</sup> Cf. US DoJ (1984). Despite their categorisation under the “non-horizontal” merger guidelines such mergers now tend to be regarded and analysed as horizontal mergers, cf. Kolasky (2001), p. 1.

<sup>18</sup> Cf. Emch (2004), p. 75 ff.

<sup>19</sup> Cf. In particular OECD (2002), p. 213 ff., Kolasky (2001).

<sup>20</sup> Cf. Kolasky (2001), page 1.

<sup>21</sup> Cf. Kolasky (2001), p. 25



## 2. The practice within the European Union

For an understanding of the Commission's recent decision practice the two merger cases GE / Honeywell<sup>22</sup> and Tetra Laval / Sidel<sup>23</sup> are of great significance.

### *Tetra Laval / Sidel*

In 2001 the merger between Tetra Laval and Sidel was notified to the Commission. According to Commission's assessment Tetra Laval was dominant in the market for the manufacture of equipment for aseptic carton packaging used, among others, for the filling of various drinks. The mechanical engineering company Sidel is a major producer of so-called SBM machines<sup>24</sup> used to manufacture PET bottles for carbonated drinks. The Commission concluded that carton and PET packaging are two separate markets. It saw evidence of a conceivable convergence between PET and carton packaging in the case of certain drinks. This found its expression in the markets for the manufacture of SBM machines and machines for the production of aseptic carton packaging. Possible substitutional relationships between the markets could therefore not be ruled out and, according to the Commission, the imperfect substitution by Sidel had a disciplinary effect on Tetra Laval.

The Commission also pointed out that the merger made it possible for Tetra Laval to transfer its dominant position on the market for the manufacture of machines for aseptic carton packaging to the market for the manufacture of SBM machines. Tetra Laval had the possibility as well as the incentive to do this due to its possible substitutional relationship. The Commission identified several mechanisms which could have such a leverage effect. As Tetra Laval operated not only as a machine manufacturer but also as a supplier of carton products, it had an information advantage over its competitors and so was in a position to better predict the

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<sup>22</sup> Cf. Commission GE/Honeywell, M.2220 of 3.7.2001=WuW/E EU-V 631 (Decision GE/Honeywell); Court of First Instance, judgement of 14.12.2005, Slg. 2005 p. II-0000 = WuW/E EU-R 977 (Court of First Instance GE/Honeywell).

<sup>23</sup> Cf. Commission Tetra Laval / Sidel, M.2416 of 30.10.2001=WuW/E EU-V 711 (Decision Tetra Laval / Sidel); Court of First Instance, judgement of 25.10.2002, Slg. 2002 p. II-4381=WuW/E EU-R 585 (Court of First Instance Tetra Laval / Sidel); confirmed by the ECJ, judgement of 15.2.2005, Slg. 2005 p. I-987=WuW/EU-R 875 (ECJ Tetra Laval/ Sidel).

<sup>24</sup> SBM machines ("stretch blow molding" machines) are used in the production of PET bottles.

customer strategy and to react accordingly. Furthermore, Tetra Laval could make use of the fact that even in the event of gradual substitution towards SBM machines a customer would have to continue purchasing carton products for his existing machinery. As a consequence Tetra Laval would be able to tie its offer of SBM machines to that of carton products. As the customers were dependent on Tetra Laval for the supply of carton products a rejection of these bundle offers was unlikely. Moreover, Tetra Laval's dominant position on the market for the manufacture of machines for aseptic carton packaging would be strengthened because of the elimination of Sidel as a potential competitor. For this reason the project was to be prohibited.

The parties to the merger successfully filed an appeal against the Commission's decision before the Court of First Instance.<sup>25</sup> In its judgement the Court of First Instance raised demands on the qualitative content of the economic argumentation. According to the court the Commission had powers of discretion and judgement in assessing economic issues. However, it had to clarify all the circumstances of a case, take account of them and, in particular, to present convincing evidence for prohibition. The Commission had to prove the basis for a prohibition, namely that the conglomerate effects would most likely create or strengthen a dominant position in the near future and would thereby significantly impede effective competition in the market concerned. This assessment should also take account of all incentive and deterrent factors. In particular, the anti-competitive behaviour must be economically rational and effective, i.e. actually lead to an increase in market power.<sup>26</sup> During the proceedings Tetra Laval and Sidel had agreed not to make joint offers for carton products and SBM machines and not to grant their customers any form of discount not justified by an objective consideration. The Commission had to consider that the potential to transfer market power was limited.<sup>27</sup> Furthermore, a tying strategy was not apt to secure a dominant position because the possibility of competitors to react to anticompetitive behaviour also had to be considered in weighing up the aspects of the case. The Court of First Instance annulled the prohibition decision. The

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<sup>25</sup> The Court of First Instance quashed the prohibition by the Commission. The Commission then cleared the merger subject to obligations.

<sup>26</sup> Court of First Instance Tetra Laval / Sidel para. 153 ff.

<sup>27</sup> Court of First Instance Tetra Laval / Sidel para. 224.

Commission finally cleared the merger subject to conditions. The European Court of Justice has confirmed the court ruling in essence.<sup>28</sup>

In consideration of all incentive and deterrent effects it was also controversial whether the deterrent effect of Art. 82 EC had to be considered. The Court of First Instance initially approved such a consideration but the European Court of Justice considered this as running counter to the preventative purpose of merger control if the Commission had to examine all possible types of conduct and the probability of their punishment. Following the judgement of the Court of First Instance in the GE/Honeywell case, which is ambiguous in the application of this criterion by the European Court of Justice, this aspect has become the subject of dispute among experts.<sup>29</sup>

### *GE / Honeywell*

In 2001 the merger between General Electric and Honeywell was notified to the Department of Justice as well as the Commission. Whereas the Department of Justice had no competitive concerns about the merger, it was prohibited by the Commission. GE is a major supplier of jet engines for commercial airlines, Honeywell is a manufacturer of aircraft components and jet engines for smaller aircraft. In the Commission decision horizontal overlaps and vertical market foreclosure effects played only a secondary role. In the Commission's view the conglomerate effects of the merger, in particular, were of concern.

In its view GE and Honeywell would jointly have been in a position after the merger to improve their market position in the respective markets through tying and bundling strategies. In the markets for aircraft components, in which Honeywell was mainly active as a strong but not dominant company, the merger could have enabled the conglomerate to provide bundles of components and jet engines with significant discounts. In the light of GE's outstanding financial power, which would make a cross-subsidisation of components probable, the conglomerate would have a competitive advantage over non-integrated competitors. In the Commission's view this would also offer it the possibility in the short or medium term to develop

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<sup>28</sup> As regards consideration of the deterrent effect under Art. 82 EC compare Section D.

<sup>29</sup> cf. Bonin (2006), Scheffler (2005).

technically coordinated components. GE / Honeywell would then be in a position to transfer GE's existing dominant position to Honeywell's markets. The result would be falls in profit for competitors and market exits, which ultimately would considerably reduce competition in these markets. In the markets for the manufacture of turbines, in which GE is already dominant, the merger would strengthen this position of dominance since tying transactions are likely to have market foreclosure effects. As the competitors would not be able to counter this strategy competitively this would strengthen GE's dominant position.

Despite abandoning the merger project following prohibition the parties to the merger took legal action against the Commission's decision. The Court of First Instance rejected the appeal because the prohibition was already justified by the horizontal and vertical effects of the merger. However, as regards the conglomerate effects, the Commission had failed to prove the creation or strengthening of a dominant position. The Commission had therefore only signified the possibility of a tying strategy in its prohibition decision. In doing so it had failed to prove whether such a strategy was likely as a result of the economic incentives of the parties to the merger. In the court dispute this issue became the subject of controversial discussion. Irrespective of a conclusive evaluation of the individual arguments the court saw this as an indication that the Commission had not furnished proof of this and had omitted to prove that the effects it claimed were a direct, logical and probable consequence of the merger. In evaluating the conglomerate effects the Commission had thus made obvious errors. The judgement is final.

### *Merger control practice following these judgements*

In the GE / Amersham case<sup>30</sup> the Commission examined whether complementary products would enable the companies concerned to transfer their market power in one product market to a second one by means of bundling strategies. Bundling strategies could only have market foreclosure effects if firstly, a dominant company were in a position to transfer its market power to a second market, secondly its competitors were not in a position to react accordingly and subsequently leave the market, and, thirdly, if this enabled the dominant company to raise prices on a

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<sup>30</sup> Commission GE/Amersham, M.3004 of 21.1.2004

permanent basis. The Commission's answer was negative. Although the parties to the merger held high market shares in some Member States, this alone was not proof of the existence of a dominant position. In addition, the Commission thought that the competitors were able to appropriately react to bundling strategies. Their exit from the market was therefore unlikely. Due to the low barriers to market entry a dominant company would also not be able to raise prices permanently. The Commission therefore comes to the conclusion that although bundling strategies are indeed possible, these can be considered as being of no competitive concern. Also the technical coordination of complementary products which could be used to squeeze competitors out of the market, was not feasible in the markets concerned. The merger was therefore cleared.

In the Johnson&Johnson / Guidant case<sup>31</sup> the Commission examined foreclosure effects resulting from bundling practices. The ability to successfully bundle complementary products was already called into question in view of the demand situation in the markets concerned. In addition, the Commission considered the other market players able to appropriately react to such strategies. Equally, in the Saint-Gobain / BPB case<sup>32</sup> the Commission came to similar results with regard to the possibility of bundling strategies in the markets of several Member States.

### **3. The practice in Germany**

According to the legislative intent of the second Amendment to the ARC, which introduced merger control into the Act in 1973, the legislator was of the opinion that "vertical and diagonal concentrations should be included in the evaluation as equal means to create or strengthen a dominant position in a market".<sup>33</sup> According to the legislator, the strengthening of a dominant position was also possible without the occurrence of a market share addition, if e.g. the merger resulted in an increase in financial power, made a resurgence of competition less likely or led to the elimination of a potential competitor.<sup>34</sup>

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<sup>31</sup> Commission Johnson&Johnson / Guidant, M.3687 of 25.8.2005.

<sup>32</sup> Commission Saint-Gobain / BPB, M.3943 of 9.11.2005.

<sup>33</sup> Bundesrat Doc. 265/71, p. 30, right column.

<sup>34</sup> Bundesrat Doc. 265/71, p. 30, left column.

In the fourth Amendment to the ARC in 1978 the legislator went even further: To make it easier for the Bundeskartellamt to prove the creation or strengthening of a dominant position in the case of vertical or conglomerate mergers, the legislator introduced additional quantitative criteria for presuming market dominance. The presumption criteria were laid down in Section 23 a (1) of the ARC (old version). They focused on penetration, combination and size and provided for the following:

“...for merger control purposes a paramount market position shall be presumed to be created or strengthened as a result of a merger, if

1. an enterprise which recorded a turnover of at least DM 2,000 million in the last completed business year preceding the merger merges with another enterprise which
  - a) operates in a market in which small and medium-sized enterprises have a combined market share of at least two-thirds and the enterprises participating in the merger have a combined market share of at least 5 per cent, or
  - b) is market-dominating in one or several markets which in the last completed calendar year had a turnover of at least DM 100 million, or
2. the enterprises participating in the merger recorded a combined turnover of at least DM 10,000 million in the last completed business year preceding the merger and at least two of the participating enterprises recorded individual turnovers of at least DM 1,000 million; this presumption shall not apply insofar as the merger also satisfies the conditions of Section 23 (2) No.2 sentence 3 and the joint venture does not operate in a market with a turnover of at least DM 500 million in the last calendar year.”

However, these rebuttable quantitative presumptions of dominance did not meet up with the expectations placed in them<sup>35</sup> because they were constantly disproved. They were therefore deleted in the 6<sup>th</sup> Amendment to the ARC which came into force on 1 January 1999.

In its case practice to date the Bundeskartellamt has mainly based its assessment of whether a conglomerate merger will lead to the creation or strengthening of a dominant position on the questions of whether or not the merger will increase financial power, improve access to sales markets or discourage potential competitors.

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<sup>35</sup> Cf. for example Niederleithinger “Die Praxis der deutschen Fusionskontrolle bei konglomeraten Zusammenschlüssen“ (the practice of German merger control in the case of conglomerate mergers) in Festschrift für Friedrich Frhr. v. Gamm, p. 637, 646; Monopolies Commission, main opinion 1982/1983, para 767.

### *Financial power*

The aspect of “financial power“ played a decisive role in the Bundeskartellamt’s decision in the GKN/Sachs case of 12 May 1976.<sup>36</sup> In its decision the BkartA prohibited the British Guest, Keen & Nettlefolds group (GKN) from acquiring shares in Sachs AG. According to the Bundeskartellamt’s findings, the company Fichtel & Sachs, which was an affiliate of Sachs AG, held market shares of over 70 per cent in the markets for the supply of clutch thrust plates and clutch disks to automobile manufacturers. In the Bundeskartellamt’s view this dominant position would have been strengthened by the concentration because it would have significantly increased the financial power behind the dominant position which in turn would have significantly broadened the scope for action of the undertaking towards customers and competitors. This would have made it more difficult for potential competitors to enter the market. According to the Bundeskartellamt it was not relevant whether the companies really intended to use their financial power to squeeze competitors out of the market or discourage potential competitors to enter the market.<sup>37</sup>

While the Federal Court of Justice confirmed the prohibition decision, it did not consider increased financial power alone a sufficient reason to assume a per se increase in deterrent potential.<sup>38</sup> In the Federal Court of Justice’s view Sachs AG would “through its integration into a highly conglomerated large-scale enterprise with significant financial power be more motivated and determined to fend off price competition than it would be as an independent enterprise. The different business policy and market strategies alone are a reason to expect this.”<sup>39</sup> The dominant position of Sachs AG, which was based on stable, exceptionally high market shares and significant barriers to market entry, would be strengthened if it were integrated into the financially strong, highly conglomerated GKN group. Finally, the Federal Court of Justice considered the fact that GKN as the acquiring company achieved 40 per cent of its turnover “close to the market” an important aspect.

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<sup>36</sup> BkartA, WuW/E BkartA 1625 ff.

<sup>37</sup> BkartA, WuW/E BkartA 1625, 1629.

<sup>38</sup> BGH (Federal Court of Justice) WuW/E 1501, 1506 – Kfz Kupplungen.

<sup>39</sup> BGH WuW/E loc. cit., p. 1510.

The strengthening of a dominant position through increased financial power also played a decisive role in the Rheinmetall/WMF case in 1989.<sup>40</sup> In this case the Bundeskartellamt came to the conclusion that the acquiring company was pursuing a systematic diversification strategy by merging with companies operating close to the market and in the acquiring company's competitive environment. Thus, Rheinmetall was expanding into business areas in which it had previously not been active. Therefore it was to be expected that its financial resources would in future be available to WMF which was already dominant in the market for stainless steel cutlery. The Federal Court of Justice ultimately endorsed the decision.<sup>41</sup>

Increase in financial strength did not play a decisive role in the Zweite T-Telematik Venture Beteiligungsgesellschaft mbH/Nexnet GmbH case.<sup>42</sup> In 2001, the company, which belongs to the Deutsche Telekom AG group, notified the acquisition of a minority stake in Nexnet, a company which provides billing services for telecommunication services. The question of whether it was to be feared that the financial strength of Deutsche Telekom behind the acquiring company would lead to the creation of a dominant position was denied in view of the fact that the affected market was young and still developing. In fact, the market had only recently been opened up by a decision of the Regulatory Authority for Posts and Telecommunications (RegTP) of 21 February 2000 on the collection of fees for telecommunication services. Access to financial power alone was not considered sufficient cause to expect a foreclosure of a market which is still in its formation phase. Another question which arose in the course of the proceedings was whether the concentration might lead to a privileged supply of Nexnet with data required for the billing services. However, since Telekom is under legal obligation (Section 33 Telecommunications Act) to provide all competitors with data in a non-discriminatory way it could not be assumed in the merger control proceedings that Telekom would violate the prohibition of discriminatory practices on a permanent basis. The concentration was therefore cleared.

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<sup>40</sup> BkartA WuW/E 1867 ff.

<sup>41</sup> BGH WuW/E 2150, 2157 – Edelstahlbestecke (stainless steel cutlery).

<sup>42</sup> Available at [www.bundeskartellamt.de/wDeutsch/download/pdf/Fusion/Fusion02/B7\\_206\\_01.pdf](http://www.bundeskartellamt.de/wDeutsch/download/pdf/Fusion/Fusion02/B7_206_01.pdf).



### *Portfolio effects*

The aspect of “product range extension” was decisive for the Bundeskartellamt’s decision in the Getinge/Heraeus case. The merger proceedings concerned the planned acquisition of Heraeus Medical Division by Getinge Industrier AB, which was notified in 2001. Even before the merger, Getinge was the leading provider of operating table systems. In the Bundeskartellamt’s view this dominant position would have been strengthened as a result of the merger with Heraeus which was dominant in the neighbouring market for surgical lighting systems. According to the Bundeskartellamt, operating table systems and surgical lighting systems had to be assigned to very closely related product markets because they were both part of the necessary basic equipment of operating theatres, were marketed by suppliers as part of an integrated corporate policy and had the same demand structure. After the merger, the companies would have been able to offer complete product bundles for operating theatre equipment and to use their increased scope for setting prices and offering rebates to market their own products or force other competitors from the market.<sup>43</sup> In addition, the Bundeskartellamt saw a danger that the specialized trade with product bundles of other, uninvolved producers would either be largely eliminated from the market or tied more closely to the parties to the merger. Therefore, the merger was only cleared subject to conditions.

### *Coordinated effects; portfolio effects; imperfect substitution*

In its decision of 19 January 2006 the Bundeskartellamt prohibited the merger project between Springer and Pro7Sat.1 (P7S1) because it was to be expected that the merger would strengthen the dominant position of the merging companies in three national markets: the TV advertising market, the reader market for over-the-counter newspapers and the advertising market for newspapers<sup>44</sup>. The decision is not yet final.

According to the Bundeskartellamt’s findings, the RTL group, which belongs to the Bertelsmann group, and the P7S1 group held a joint dominant position in the TV advertising market even before the merger. The scope for action of this duopoly,

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<sup>43</sup> Bundeskartellamt WuW DE-V 669, 671.

<sup>44</sup> Available at [www.bundeskartellamt.de/wDeutsch/download/pdf/Fusion/Fusion06/B6\\_103\\_05.pdf](http://www.bundeskartellamt.de/wDeutsch/download/pdf/Fusion/Fusion06/B6_103_05.pdf).

which together held approx. 80 per cent of the market shares, was not limited by effective competition, either internal or external. This duopolistic dominant position would have been further strengthened by the merger. According to the Bundeskartellamt, the merger would also have led to a further structural harmonisation of the two broadcasting groups that were already interlinked through several joint ventures. This would have increased the number of business areas where there was a potential for retaliation against the other duopolist. In addition, both company groups would have gained the possibility to offer cross-media advertising campaigns from one source. Furthermore, the BILD newspaper, which until then had been the only alternative to national TV advertising, would have lost this substitute function.

The Bundeskartellamt continued to explain in its decision that the BILD newspaper, which is published by Springer, had held a dominant position on the reader market for over-the-counter newspapers for decades. Following the merger, this dominant position would have been secured by cross-media promotion in the form of reciprocal advertising. In addition, the duopolists would have gained the possibility to offer one another advertising facilities at prices below the usual market rate. Moreover, there would have been the possibility of so-called editorial cross-promotion, whereby for example BILD could have been promoted in TV programmes on P7S1. The Bundeskartellamt saw the main advantage of editorial cross promotion in that TV viewers generally placed more trust in editorial programmes than in advertising blocks, which was one of the reasons why this type of advertising was particularly effective. Also, improved sales opportunities for BILD would have raised barriers to market entry and consequently deterred potential competitors.

Finally, the merger would also have strengthened the acquiring company's dominant position in the national advertising market for newspapers in which it was already the market leader. This was to be expected because the dominance of the acquirer could have been strengthened by cross-media advertising campaigns. The same was true of its dominant position in the TV advertising market.

#### **4. Summary of the most significant results**

Since the 1980s, U.S. practice has been to adopt an open attitude towards conglomerate mergers. Conglomerate mergers are assumed to have significant efficiency potential. Although they may in principle also have anti-competitive effects, such effects may only occur if a number of prerequisites are given. To prove these effects would require speculative predictions about the future conduct of market participants. Since the risk of making wrong prohibition decisions is high, competition authorities are urged only to take action against conglomerate mergers if these eliminate potential competition. To avoid anti-competitive effects, an ex-post control within the framework of abuse control is given priority over ex-ante control within the framework of merger control.

Following the decisions of the ECJ and the Court of First Instance in the merger control proceedings Tetra Laval / Sidel and GE / Honeywell, the Commission's practice is currently undergoing a change. It is evident from these decisions and the Commission's decisions that have followed since, that in principle the Commission considers merger control to be important also in the case of conglomerate mergers. The courts are of the opinion that since conglomerate mergers are hardly likely to have anti-competitive effects a prohibition decision in a conglomerate merger case would have to be based on sound economic analysis. According to them, it has to be proved in merger control examinations that under consideration of the prohibition of abusive behaviour and all economic incentives, anti-competitive behaviour is likely and will de facto impair competition.

The view of the historical German legislator that conglomerate mergers largely pose as great a threat to competition as horizontal mergers does not correspond with the practice of the Bundeskartellamt. So far, conglomerate mergers have only been prohibited in a few exceptional cases. The substantive evaluation of these mergers focused mainly on structural aspects. Other than in the United States and the EU, courts in Germany have confirmed in essence the Bundeskartellamt decisions.

## **C. Conglomerate mergers seen from an economic perspective**

Unilateral or non-coordinated merger effects are those that result from a change in individual incentives and the likely reactions of all market participants to this change while the strategic interaction between market participants remains unaffected. Coordinated effects on the other hand are those effects that result from a change in the strategic interaction between companies in that the companies restrict their competitive activities for the sake of mutual coordination. Such coordination can also be reached without explicit agreement.

### **1. Unilateral effects**

A number of unilateral effects are unobjectionable from a competition point of view since they increase efficiency and do not impede effective competition. Under certain conditions, however, conglomerate mergers may also have anticompetitive effects. The effects mostly discussed in this context are the so-called portfolio effects. Other significant unilateral effects are those that may arise through the elimination of imperfect substitution or potential competition and through an increase in financial strength.

#### *Effects that are unobjectionable under competition law*

Conglomerate mergers may lead to the realisation of economies of scale and scope. Economies of scale and scope occur when the joint production of several goods is cheaper than the production of the same goods in separate corporate entities. Where economies of scale and scope occur, the merger enables the companies to realise cost savings. Cost savings increase the efficiency of companies and tend to result in lower prices, a better supply of markets and higher welfare. It has to be noted that this effect is not the result of increased competitive pressure but merely results from a change in the profit maximization calculation due to a reduction of marginal costs.

Conglomerate mergers offer an opportunity for companies to spread risks more evenly within the company structure. This is the case where the merger involves

business entities that are characterised by diametrically opposed risk cycles, e.g. due to differing dependencies on the demand and production side. Risk balancing has positive effects on a company's financial possibilities which in turn increases its capacity for innovation and its efficiency. Improved possibilities of refinancing through the capital markets, however, may also be used to squeeze competitors out of the market (see below).

Where the products manufactured by the parties to the merger are interdependent, an integration of the companies may be efficiency-enhancing. This is the case where, e.g., a technical coordination of products can increase their utility value for customers. Where such product coordination requires specific investment, in a "market solution" companies may be reluctant to undertake such investment or may only invest an inefficient amount to avoid any dependence on other market participants. This inefficient investment behaviour, which is referred to as the "hold up problem", can be overcome by integrating the companies concerned because all investment revenue following the merger is accrued within the merged company, i.e. positive external effects of the investment are internalised.

Where individual products have positive external effects on one another, i.e. the benefit from the consumption of one product has a positive impact on the utility value of another, an integration may lead to an efficient market solution and lower prices. This is so because the company internalises the external effects which could not be compensated through market mechanisms. This is also the case where products complement one another in their utility. In such a case the positive effect which lower prices have on demand in the other market will be internalised as a result of the merger, which in turn tends to lead to lower prices.

### *Portfolio effects*

Portfolio effects are unilateral merger effects which can result from the expansion of a company's product range as a consequence of a merger. The combination of different complementary products can above all change the incentives to market these as tied or bundled offers.<sup>45</sup> The theory of portfolio effects is thus largely based

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<sup>45</sup> For up-to-date overviews of literature on this topic see e.g. Kobayashi (2005), Carlton and Waldmann (2005).

on the findings on incentives and effects of tying and bundling practices. Irrespective of the possible negative effects discussed below a portfolio expansion can lead to increased consumer welfare due to various mechanisms.

About 30 years ago the Chicago School's view still prevailed according to which no anticompetitive portfolio effects can emerge.<sup>46</sup> This view was based on a comparative static model which was meant to prove that tying could not lead to exclusionary profits so that tying practices for purely exclusionary purposes would be irrational. The model's crucial assumption is that perfect competition exists for the tied product without any entry barriers. Before the tied offer is made the competitive product is thus offered at the marginal cost price and another monopoly product at the monopoly price. When the products are tied the monopoly product is no longer available as a separate product, but only the tied offer or the competitive product alone can be purchased. However, the price of the tied offer may not exceed the sum of the previous unit prices as otherwise the company would reduce its profit. In other words, the full monopoly profit was already achieved through the monopoly prices charged prior to the tying strategy. From this model the Chicago School draws the conclusion that bundled offers which can be observed in reality are exclusively based on efficiencies which increase both corporate profits and consumer welfare. Under different preconditions, particularly in a dynamic analysis and if there are entry barriers, this conclusion does not hold.

An important shortcoming in the conclusions of the Chicago School is first of all that under this model absolutely no costs are involved in squeezing competitors out of the market. If, e.g., the two products concerned are consumed by customers exclusively in fixed proportion, the conglomerate company can occupy the total volume of the competitive market by combining the two products in this way. Although this conduct will not result in additional profits for the company in the short term, the company is in a position to monopolise the competitive market without having to incur any costs in squeezing out its competitors. If the two products are not consumed in fixed proportions, a mixed bundle or a bundle discount is even profitable for the conglomerate company on a short-term basis, irrespective of possible additional

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<sup>46</sup> cf. e.g. Bork (1978), p. 372 ff., Posner (1976).

profits in the future.<sup>47</sup> Under this model, the fact that, in contrast to cut-price strategies, no costs are involved in squeezing competitors out of the market through tying or bundling measures, allows the conclusion that tying or bundling measures are generally a very promising exclusionary strategy.<sup>48</sup> If the assumption of no entry barriers is abandoned, the model leads to the conclusion that exclusionary profits arise in the long term.

Under certain conditions competitors can be prevented from entering the market by tying and bundling strategies. A precondition is that competitors are unable to enter both markets (or that this entry would be unprofitable). A company can prevent competitors from entering the market e.g. by committing to continue to bundle the two products.<sup>49</sup> Such a credible commitment to continue bundling practices are e.g. technical integration measures or the fact that bundling would in any case be the best reaction to a possible market entry.<sup>50</sup> In the case of entry into one of the two markets, a loss of sales in one market would result in a corresponding loss in the second market due to the bundling strategy. As the company would maintain its bundling practice, a market entry would cause it to suffer a relatively high loss. The company would therefore react to the entry by adopting an aggressive pricing policy. Market entry can thus become unprofitable, which keeps potential competitors from entering any one of the two markets. This strategy is all the more successful if more products are included in the bundle.<sup>51</sup> Tying and bundling strategies for the purpose of preventing market entries will be particularly profitable for the company concerned if an entry into the adjacent markets takes place sequentially, i.e. if one of the markets concerned can serve as an entry point into the other market and/or if economies of scale or network effects exist in the markets.<sup>52</sup>

Similar to the prevention of market entry, the credible continuation of tying and bundling practices may also result in a reduction of innovative activity.<sup>53</sup> This can be the case if the bundling strategy provides the conglomerate company with an additional incentive to invest in research and development. Provided that the

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<sup>47</sup> This is due to the reduction of the monopoly price's inefficiency which is possible because of the variable proportions in which the products are consumed. For a formal proof see Nalebuff (2004), Greenlee et al. (2004).

<sup>48</sup> cf. Nalebuff (2004).

<sup>49</sup> cf. Whinston (1990).

<sup>50</sup> For situations in which this is the case, see Nalebuff (1999).

<sup>51</sup> cf. Nalebuff (2000).

<sup>52</sup> cf. Carlton and Waldmann (2002).

<sup>53</sup> cf. Choi and Stefanadis (2001), Choi (2004).

competitors react to such a strategy by reducing their own innovative activities, all R&D investments could decrease in the market concerned. If, however, competitors step up their own innovative activity in reaction to this development, overall investment will rise.

Portfolio effects can also occur as a consequence of the product range extension itself.<sup>54</sup> This can be the case if customers appreciate the diversity or breadth of a product range. If competitors are merely able to offer lower product diversity, this could possibly lead to exclusionary effects. In this case, however, the possible long-term exclusionary effects on the one hand are contrasted by a positive effect on consumer welfare on the other which results from the broader range of products.

#### *Elimination of imperfect substitution*

If, although they are seen as belonging to different product markets, the products of the parties to the merger can to some extent be substituted for one another, the elimination of imperfect substitution can cause unilateral effects. The products of the respective relevant markets differ slightly from the imperfect substitutes in that they can either only be replaced by them to a limited extent or subject to certain conditions.<sup>55</sup> Even though imperfect substitutes as a rule cannot sufficiently control a dominant company's scope of action they can restrict it to some extent. Depending on the scope of substitution the elimination of imperfect substitution can thus lead to unilateral effects. From an economic point of view the analysis of the unilateral effects of the elimination of imperfect substitution is basically the same as in the case of horizontal mergers, so that corresponding oligopoly models can be used.<sup>56</sup>

#### *Elimination of potential competition*

Unilateral effects can also occur if a potential competitor is eliminated by the merger. The theory of contestable markets illustrates how potential competition can have a disciplinary effect. If potential competitors can enter a market immediately and without sunk costs, a (hypothetical) monopolist is forced to supply at the competitive

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<sup>54</sup> cf. Church (2004), p. 219 ff.

<sup>55</sup> For various examples of possible reasons for this limited substitutability see Bundeskartellamt (2005), p. 30 f.

<sup>56</sup> For a typical illustration of the effects of marginal competition see e.g. Carlton and Perloff (1999), p. 107 ff.



price or the competitive quantity. But even if barriers to market entry exist it may be rational for a dominant company to depart from short-term profit maximisation in order to prevent market entries. This can be achieved e.g. by reducing the price level to the limit price, a strategy by which the dominant company intends to deceive potential competitors about the actual profit opportunities in the respective market.<sup>57</sup> In the same way the dominant company can also build up additional capacities to make it credible that potential competitors would not be able to generate sufficient profits to cover the costs of their potential entry.<sup>58</sup> Both practices increase consumer welfare on a short-term basis. Conversely, the elimination of a firm which the established company considered to be a potential competitor can generally lead to unilateral effects, also on a short-term basis. In the long term the elimination of a potential competitor generally leads to anticompetitive effects if this company had entered the market without the merger.

#### *Increase in financial strength*

An increase in financial strength can lead to cost reductions which usually have a positive effect on consumer welfare (see above). Under certain preconditions a consolidation of financial strength can also result in unilateral effects. This can be the case if, prior to the merger, the dominant company had only limited sources of finance and if greater financial strength thus increases its capability to carry out exclusionary strategies, in particular cut price strategies. If competitors expect that cut price strategies are likely to be used, this can lead to deterrent and discouraging effects. The analysis of whether an increase in financial strength leads to such unilateral effects is thus largely based on existing knowledge about predatory pricing.<sup>59</sup> As a rule, squeezing competitors out of the market by means of cut prices is a relatively costly strategy for dominant companies. On the other hand the renunciation of the use of cut prices can cause future costs as competitors could possibly gain market shares or enter into the market. From the dominant company's view, squeezing competitors out of the market by means of cut prices is only a rational strategy if the costs incurred during the cut-price phase are lower than those involved in a renunciation of cut prices. A number of elements play a role in this calculation. The costs of the cut price phase tend to increase with the dominant

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<sup>57</sup> On limit pricing see Tirole (1999), p. 803 ff.

<sup>58</sup> cf. Dixit (1980).

<sup>59</sup> for predatory pricing practices see Bolton et al. (2000).

company's difficulty in differentiating prices and the extent of its competitor's means of financing. The expected additional profit after an exit from the market tends to increase with the extent of barriers to market entry and with the possibility of making use of reputation effects in the market concerned and other, e.g. adjacent markets.

## **2. Coordinated effects**

Coordinated effects can occur if a merger enables the companies that are active in the markets concerned to abandon their pro-competitive behaviour and engage in tacit or explicit coordination.<sup>60</sup> Coordination can only be achieved on a permanent basis if certain preconditions are fulfilled. It has to be examined within the framework of merger control proceedings whether the merger fosters conditions that favour market coordination, i.e. whether tacit cooperation between the competitors will become more likely as a consequence of the merger.

Tacit coordination is only possible if the market participants succeed in identifying a joint market solution without any communication and implement this on a permanent basis. Since a coordinated solution, just as an explicit agreement, cannot be enforced in court, it can only be implemented on a permanent basis if none of the significant companies is interested in pulling out of the cooperation unilaterally. As soon as the market participants become aware of a company pulling out, they are also forced to act competitively from that moment on.<sup>61</sup> The volume of profit in the case of collusion or competition and the one-off gain from deviation are thus important for the consideration of whether to continue a cooperation. A coordination can only be kept up if for each company the cash value of future profits in the case of coordination is higher than the sum of the deviation profit and the cash value of future competitive profits.

Different factors have an influence on the likelihood of this condition being fulfilled. These are e.g. the extent of market concentration, the number and symmetry of the companies, demand characteristics, the extent of market transparency and the

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<sup>60</sup> Articles providing a good overview of the issue of coordination of companies can be found in Feuerstein (2005), Ivaldi et al. (2003), Motta (2004), chap. 4. This outline essentially follows these articles and the papers quoted therein.

<sup>61</sup> Switching to competitive behaviour as soon as another participant's deviation is observed is referred to as a sanction mechanism.

existence of barriers to market entry. Within the framework of the merger control examination it has to be assessed first of all how a conglomerate merger influences these factors. An overall consideration of all factors then leads to an evaluation as to whether the merger makes market coordination more likely, stable or successful. In the following some important market parameters will be discussed.

### *Potential competition and imperfect substitution*

Due to the elimination of imperfect substitution or a potential competitor a conglomerate merger could possibly have an influence on the number of companies that can influence market coordination.<sup>62</sup> A lower number of companies tends to result in lower potential profits from pulling out of a collusion. This strengthens the incentives to continue the collusion. On the other hand, the profits achieved in the ensuing competitive phase are higher with a smaller number of companies so that the disadvantage of deviation weighs less. The question of whether a lower number of companies makes collusion more likely therefore requires further differentiation.

If the companies are symmetrical the first effect is predominant, and collusion is more likely to occur. In that case the gain from deviation is so low that it would not pay off to break away from the cooperation which is why the companies maintain the joint market solution. If, however, the companies are asymmetrical, differing e.g. in their capacities or product ranges, it will be more profitable for them to break away from collusion, thus making a coordinated market solution more unlikely.<sup>63</sup>

With regard to the market concentration factor conglomerate mergers must therefore be considered in a differentiated way. If a merger reduces the number of companies in a certain market, and if these have a similar structure, the companies will be more likely to engage in tacit coordination as a result of the merger. On the other hand the

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<sup>62</sup> Bundling strategies can also cause independent suppliers to disappear from markets, which tends to reduce the number of companies.

<sup>63</sup> The question of whether large or small market participants are more likely to have an incentive to break away depends on how the companies differ from one another. If the companies are different in terms of capacity limits, only large companies will have an incentive for deviation as the capacity limits of small companies restrict their gain from deviation. If, however, the companies differ in terms of their product range, small companies tend to be more interested in deviation as this could enable them to capture a larger share of demand. Irrespective of the question as to which companies deviate, it is significant in this context that coordinated effects are more unlikely to occur in asymmetrical market structures.

elimination of potential competition is less likely to raise concerns if the companies concerned were already structured differently prior to the merger and largely maintain these structures afterwards. In the case of a merger resulting in a more heterogeneous market structure, i.e. where a symmetrical market situation becomes more differentiated after the concentration, it is even to be considered as favourable with regard to cooperative effects that fewer companies can exert an influence on the coordination. In this case the likelihood of a collective market solution decreases.

### *Effects across markets*

A conglomerate merger can increase the likelihood of coordinated effects if the merger enables the companies to include several separate markets in their consideration of a cooperation solution. This occurs either if the potential to retaliate against deviations increases as competitors confront each other in several markets after the merger, or if the market participants are faced with a problem which becomes increasingly similar as all markets are included in the consideration to enter into a cooperation. This effect can be illustrated by an example:

Assuming the symmetrical companies A and B were active in market 1 before the merger. Coordination is likely to occur in this market. Company B is also active in market 2 where it faces company C which, compared to B, has a high market share. Due to the asymmetrical structure, collusion will not take place because company B has an incentive for breaking away. As a consequence of a conglomerate merger between companies A and C the companies which are different in terms of their respective markets become more and more alike across all the markets. In terms of its structure company AC becomes similar to company B. If, before the merger, a coordination could not be achieved in market 2, the conglomerate corporate structure now creates a link between these markets. As the corporate structures become more and more similar across the markets, a cooperative solution is more likely to be achieved. The connecting link is the plan to switch to competitive behaviour in all markets if the other side of the market breaks away from the cooperative solution in one market. As both companies take this into consideration, the process of weighing up whether a cooperation is to be maintained is similar, irrespective of the individual

markets' asymmetrical structures. Due to the weighing-up process the conglomerate structure acts as a link between independent markets. As similarly structured companies have less incentives to break away from a cooperation, a conglomerate merger can increase the likelihood of a coordinated market solution.

#### *Market entry and external competition*

If market entry is possible the likelihood of a coordinated market solution decreases. If a major participant enters the market and does not join the cooperation, coordination will break down. Even under the assumption that the new market player will participate in the market coordination, this will tend to have a destabilising effect on the tacit coordination as the incentive to break away increases with the number of participants in the market. If a conglomerate merger makes market entry less attractive, e.g. due to financing aspects, economies of scope or bundling strategies, the likelihood of coordinated effects will increase. The same applies to cases where the merger results in the elimination of a potential competitor or an imperfect substitute.

#### **D. Central propositions for the future assessment of conglomerate mergers in practice**

*Under certain preconditions conglomerate mergers can have anti-competitive effects.*

Neither the view expressed by the historical legislator that the competitive threat potential of conglomerate mergers equalled that of horizontal mergers nor the Chicago School's view that conglomerate mergers were always unobjectionable are compatible with the current state of economic theory. Under limited conditions, conglomerate mergers may also have anticompetitive effects. Unilateral as well as coordinated effects can occur.

A dominant company's scope for action can increase if an important imperfect substitute is eliminated. In the same way anticompetitive effects can result from the absence of a company which would possibly have entered the market if the merger had not taken place. Portfolio effects can emerge if an expanded product range alters

the possibilities and incentives to market these products as tied or bundled offers. If, as a result of increased financial strength, the merger increases the likelihood of cut price strategies, this can lead to deterrent and discouraging effects.

*Also in the case of conglomerate mergers the prohibition of abusive practices cannot replace merger control.*

The prohibition of abusive practices can only cover part of the possible negative effects of conglomerate mergers, i.e. portfolio effects based on possible exclusionary practices and effects of financial strength. Not covered by the ban on abusive practices are the loss of potential competition and imperfect substitution, and increased coordination.

According to a view held e.g. by the US competition authorities, the private and state-imposed sanctions under the prohibition of abusive practices are generally sufficiently deterrent to prevent illegal exclusionary practices, so that in principle portfolio effects and effects of financial strength are not to be expected. The Court of First Instance's decision in the GE / Honeywell case points in a similar direction. In the opinion of the Court of First Instance, the European Commission must take the deterrent effect into account in cases of clear or most probable violations of Article 82 EC.

The hypothesis of sufficient deterrence is doubtful, however, as the number of undetected violations of competition law is unknown and the actual deterrent effect of the sanctions cannot thus be estimated reliably. Moreover, in most cases even the assessment of whether a hypothetical behaviour might violate the prohibition of abusive practices is unclear. If a competition authority were to carry out an ex-ante substantive assessment of each possible variant of abuse of power, it would soon run up against its limits. Irrespective of these practical problems, an "Article 82 defence" leads to a paradoxical result: As the most damaging hypothetical practices would be most likely to violate the ban on abusive practices, only the more harmless practices can be assumed for the purposes of an analysis under merger control law.

*If a competition authority's prohibition decision in the case of a conglomerate merger is based on future behaviour, the appropriate standard of proof is whether, from an economic point of view, this behaviour is likely to occur.*

In German practice and case law structural criteria are primarily considered, also in the examination of conglomerate mergers. The Bundeskartellamt's prohibition decisions are thus not primarily based on the participating parties' likely future behaviour, but above all on the merger's likely effects resulting from the elimination of potential competition and imperfect substitution and increased financial strength. If, in addition to this, a prohibition is also based on the participating parties' future behaviour, the standard of proof applied by the Bundeskartellamt is whether this behaviour is likely to occur. A certain behaviour is to be considered likely if it is possible and commercially reasonable.

In contrast to the German practice, the European Commission based its Tetra Laval/Sidel and GE/Honeywell decisions less on structural changes resulting from the merger and more on the future behaviour to be expected from the participating parties. In the European courts' view the European Commission has to provide convincing evidence that the predicted behaviour is likely to occur. According to the Court of First Instance, above all internal documents of the participating companies outlining their intentions and economic considerations or studies can be considered as proof. In both proceedings the European Commission was unable to meet the standard of proof required for conglomerate effects. The details contained in the opinions of the court indicate that a relatively high standard of proof was required. However, as the European Commission based its decisions primarily on the future behaviour to be expected of the participating parties (in contrast to the German practice), this different emphasis may have caused differences in the courts' assessments of the competition authorities' decisions.

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