Competition Appeal Tribunal Sets Deferential Standard for CMA Merger Control Review

02 / 19 / 20

Skadden

If you have any questions regarding the matters discussed in this memorandum, please contact the attorneys listed on the last page or call your regular Skadden contact.

Four Times Square
New York, NY 10036
212.735.3000

A recent decision by the Competition Appeal Tribunal (CAT), *Tobii AB (publ) v. Competition and Markets Authority*, confirms a deferential standard for the U.K. Competition and Markets Authority (CMA) in its merger prohibitions.

The CMA is widely regarded as a thought leader among merger control authorities. Although the U.K.'s merger control regime is technically voluntary, the CMA's mergers intelligence committee is quick to call in mergers that catch its eye, both before and after closing. The CMA has been aggressive to assert jurisdiction over foreign-to-foreign deals with little U.K. nexus and a fast adopter of theories from academia on "killer" acquisitions or innovation. Its analytical lens has extended well beyond classical antitrust analysis — *i.e.*, reviewing deals that could result in unacceptable levels of concentration or exclusion of rivals — to deploy more speculative theories, such as whether ostensibly outsized valuations mask anticompetitive intent; whether currently nascent competitors might, in fact, be future heavyweights; or whether alternative buyers generate more competitive outcomes.

The system remains a purely administrative one, where case teams (assisted by expert panels) seek to assess deals' potential competition issues against a breakneck administrative timetable. Judicial recourse is limited. The CAT is a highly specialized tribunal, but it hears appeals on mergers only under a judicial review standard: Barring illegality, irrationality or procedural impropriety, the CMA's decisions will stand. Some practitioners have observed that this standard accords merger decisions a near appeal-proof level of judicial deference.

In *Tobii*, the CAT heard a rare root-and-branch appeal on both the merits and procedure of a CMA merger prohibition. The CAT confirmed the high degree of deference accorded to the CMA, as to both factual assessments and procedural choices.

Key Takeaways

- No *de novo* or merits appeal of CMA merger decisions is available. Appellants must meet the high bar of judicial review to overturn merger decisions, showing the decision is tainted by illegality, irrationality or procedural unfairness.[1] CMA errors on core substantive issues, such as market definition or closeness of competition, will survive challenge unless so egregious as to meet the irrationality standard.
- Hard-edged legal questions provide the most fruitful prospects for challenge as demonstrated in *Eurotunnel*,[2] which involved consideration of the legal definition of an enterprise, as opposed to the acquisition of bare assets.
- Claims alleging procedural unfairness can succeed in clear cases as demonstrated in *Sainsburys/Asda*.[3] Here, the CAT struck down an impossibly short CMA deadline for responding to detailed working papers immediately before the main party hearings in the case. It held this was procedurally unfair in light of the exceptional complexity and volume of the materials and the CMA's refusal of the parties' request to extend the prenotification discussions to accommodate the extensive evidence gathering.
- Nondisclosure of underlying evidence will only exceptionally result in procedural illegality. The CAT will allow the CMA to curtail disclosure on grounds of administrative efficiency. The parties are entitled only to understand the gist of the evidence

[1] *Council of Civil Service Unions v. Minister for Civil Service*, [1985] AC 374, at 410.
[2] *Société Coopérative de Production SeaFrance SA v. The Competition and Markets Authority*, [2015] UKSC 75.
[3] *Sainsburys/Asda v. Competition Markets Authority*, [2019] CAT 1.

against them. If evidential summaries allow a fair opportunity to understand and respond to the case, no greater disclosure will be required. Underlying data, surveys or documents need not be provided.

- Successful quasi-merits style arguments based on distortion of the facts or lack of proportionality are exceptionally rare, given the very broad margin of discretion afford to the CMA and the very high threshold for showing irrationality or unreasonableness.

Tobii confirms that the CAT will be deferential to complex factual assessments when applying a judicial review standard. As the CMA embraces more speculative merger control theories, it may be asked whether a tighter standard of judicial accountability is required.

The Judgment

In *Tobii*, the CAT broadly upheld the CMA's prohibition of Tobii's acquisition of Smartbox, concluding the two communication-aids suppliers were close rivals, holding a combined 60-70% U.K. market share. The parties' communication-aids were specialist dedicated devices, but they faced a wave of competition from consumer devices — tablets fitted with suitable software and accessories — which served the majority of communications-aids users. Some evidence suggested this was a genuine constraint on dedicated devices. The parties, indeed, had launched tablet like devices with similar price points to combat this new source of competition. Online surveys commissioned by the parties — but dismissed by the CMA — also seemed to support this constraint assertion. The parties' essential challenge was that the CMA refused to acknowledge this dynamic, focusing essentially only on the purchases of National Health Service buyers, who perhaps understandably focused on dedicated devices, to the exclusion of the wider market.

Procedural Unfairness: Failure of Disclosure

The CMA did not provide disclosure of underlying evidence, including customer and competitor submissions (such as responses to CMA information requests) and call transcripts and submissions made by Smartbox. It maintained defendants were only entitled to understand the "gist" of the case to enable it to defend its interests, which could be adequately conveyed through anonymized summaries at the provisional findings stage.

The CAT held that the CMA owes a duty of procedural fairness but is not obliged to provide all evidence received or disclosure prior to releasing its provisional findings.[4] At the provisional findings stage, according to the CAT, the CMA was not required to do more than provide summaries of the relevant customer/competitor questionnaires, anonymized customer responses and target submissions. Only the gist of the case the defendants have to answer, not the actual underlying materials, must be disclosed. To require more would negatively impact the efficiency of the procedure and deter third-party submissions. In fact, Tobii had made a detailed, on-point reply to the provisional findings, demonstrating there had been no unfairness.

Irrationality: Evidence Collection

Tobii asserted that the CMA made material errors in its evidence collection. The CMA maintained that it had taken all reasonable steps to understand the relevant information and that the totality of evidence relied upon was relevant, reliable and consistent.

The CAT held that the relevant legal test is the ordinary domestic standard of rationality ("irrationality").[5] The CMA has a wide margin of discretion when evaluating factual evidence, and therefore there "needs to be a strong case to show that the [CMA] has manifestly drawn the line in the wrong place."[6] The evidence does not need to be perfect, and a simple error by itself is not irrational if not material overall.

Consequently, the CAT found that it was not irrational for the CMA to solicit feedback from only institutional customers, as they represented approximately 90% of the parties' customer

[4] See, *e.g.*, *Ryanair Holdings PLC v. Competition Commission* [2014] CAT 3 (*Ryanair*), para. 116 "Fairness is an evolving concept . . . . It is a basic principle of administrative law recognized in many reported decisions. In *O'Reilly v. Mackman* [1983] 2 AC 237 at 279F-G, Lord Diplock rightly emphasized the fundamental nature of the right afforded by the rules of natural justice or fairness, namely to have afforded to the person concerned 'a reasonable opportunity of learning what is alleged against him and of putting forward his own case in answer to it.'"

[5] *Tobii*, para. 49, relying on *BAA Limited v. Competition Commission* [2012] CAT 3 (BAA), para. 20(5). The rationality test requires that the decision-maker had a sufficient basis in light of the totality of the evidence available to it for making the assessments. It refers to a situation where the decision is so unreasonable that no decision-maker, properly instructed and taking into account all relevant considerations, could make it. It requires an assessment of whether the conclusions are adequately supported by the evidence, whether the facts have been properly determined and whether all materials facts have been taken into account.

[6] *Tobii*, para. 183, citing in support *Akzo Nobel N.V. v. Competition Commission* [2013] CAT 13.

sales. Similarly, the CMA did not have to consider Tobii's dedicated end-user survey, as it had articulated clear reasons for rejecting it. The customer questionnaires were reasonable, since the CMA had taken steps when designing them to reduce the risk of bias or misleading responses. Finally, calculating diversion ratios based on a small subset of NHS customer data was reasonable, as the CMA also cross-checked the diversion data against a range of other qualitative and quantitative evidence, including the merging parties' own sales data.

Irrationality: Market Definition

The CAT held that the CMA acted rationally in defining a market for dedicated communications aids to the exclusion of consumer devices. The CAT held that the rationality standard does not require it to reassess the relative weight given to different evidentiary factors or to trawl through the CMA's analysis to identify arguable errors. The CAT's only inquiry is whether the CMA had "a sufficient basis, in light of the totality of the evidence available to it," for reaching its final decision.[7]

On this basis, it was reasonable for the CMA to disregard the *SSNIP* test since its theory of harm is not primarily concerned with price increases but rather with reduction in quality and/or choice of products and the level of innovation, the CAT ruled. Additionally, the CMA decision to not review substitutability on a product-to-product level was reasonable. While this approach did not "necessarily [reflect] the diversity and richness of competition between differentiated products," the CMA verified the results using a range of other evidentiary sources, and there was no inconsistency.

The CAT was, however, prepared to fault the CMA for including one of the parties' products within its posited market for dedicated devices. Tobii's Indi product — one designed specifically to respond to the threat of consumer tablets — fell outside the relevant product market, having functionality and a price point similar to consumer products. The CMA's conclusion was not supported by the available evidence. However, this error was not material since Indi's inclusion did not have an impact on the market share or diversion analysis, as highlighted by the CMA in its final report. Consequently, it is not sufficient to identify an error of assessment. The merging party also must demonstrate that, but for this error, the CMA could have reached a different conclusion.

Irrationality: SLC Finding Based on Horizontal Foreclosure Not Supported by Evidence

Tobii asserted that the CMA made material errors in its substantial lessening of competition (SLC) assessment, since the evidence relied upon was not reliable or credible. The CMA maintained that it is a matter of discretion whether the body of evidence is sufficient to justify an SLC conclusion and so falls outside the scope of judicial review.

The CAT confirmed that the CMA must apply a "probabilistic test" to determine whether, after a full and proper consideration of the available evidence, it is satisfied on the balance of probabilities that the transaction is likely to cause an SLC.[8]

On this basis, the CAT rejected Tobii's argument that the total body of evidence from customers, competitors and the merging parties' internal documents was, individually and/or collectively, insufficient to underpin an SLC finding. The CMA considered a range of evidentiary sources. Its conclusion was based "not on any single category of evidence in isolation, but on all the evidence taken together."[9] The judicial review standard only required the CAT to confirm that "there was some evidence on which to base [the CMA] decision," but it's for the CMA "to weigh up the totality of the evidence" available to it and conclude it was sufficient to ground its SLC findings.[10] The CMA was not operating in an "evidential void." It relied upon a range of data sources and verified its initial analysis by cross-checking against both qualitative and quantitative data sources. Tobii's "granular arguments" regarding, *inter alia*, particular questions put to customers and competitors was not sufficient to establish that the CMA's evaluation of the "totality of the evidence" was unreasonable or irrational.[11] Furthermore, while the CMA's inclusion of the Indi product in relevant market analysis added "unnecessary and avoidable uncertainty" to the CMA's assessment, it was not a material error, as it did not have a meaningful impact on the overall analysis or final SLC conclusions.[12]

[7] *Tobii*, para. 329, citing *BAA* and *British Sky Broadcasting Group PLC v. The Competition Commission and The Secretary of State for Business, Enterprise and Regulatory Reform* [2008] CAT 25 (*BSkyB*) judgments in support.

[8] *Tobii*, para. 341, citing *BSkyB* in support.

[9] *Tobii*, para. 361.

[10] *Tobii*, para. 365.

[11] *Tobii*, para. 367.

[12] *Tobii*, para. 380.

Competition Appeal Tribunal Sets Deferential Standard for CMA Merger Control Review

Irrationality: Vertical Foreclosure Analysis Not Supported by Evidence

The CAT partially upheld Tobii's fifth ground of appeal. Tobii argued the CMA had no reasonable basis for its input foreclosure theory. The CMA held the merged entity could partially foreclose rivals by either increasing the wholesale price of Smartbox's Grid software for downstream competitors and/or by degrading rivals' access to the Grid software by refusing to support their hardware and thereby making them less competitive for end customers. However, the available evidence the CMA had reviewed related only to a situation in which the competition concern was based on a total foreclosure strategy, where the rivals could no longer offer the Grid software as part of their dedicated communication-aids solutions.

The CAT found the CMA acted irrationally. It was unreasonable for the CMA to not try to obtain evidence as to what impact a wholesale price increase would have on the merged entity's downstream rivals. This was particularly egregious, according to the CAT, given that the evidence on file indicated that at least one downstream rival had absorbed a recent wholesale price increase, rather than pass it on to the end customers, which contradicted the CMA's partial foreclosure theory of harm. Furthermore, the CMA had not obtained any evidence or conducted any economic analysis to identify whether such a partial foreclosure strategy would be profitable for the merged entity. Therefore, the totality of the evidence did not support a conclusion that the merged entity had the ability and/or incentive to engage in a partial foreclosure strategy. This was a clear case where the evidence available on the file did not support the CMA's specific theory of harm.

Contacts

Bill Batchelor
Partner / London
207.519.7312
bill.batchelor@skadden.com

Frederic Depoortere
Partner / Brussels
322.639.0334
frederic.depoortere@skadden.com

Giorgio Motta
Partner / Brussels
322.639.0314
giorgio.motta@skadden.com

Ingrid Vandenborre
Partner / Brussels
322.639.0336
ingrid.vandenborre@skadden.com

Melissa Healy
Associate / Brussels
322.639.0337
melissa.healy@skadden.com