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CFI Overturns Commission Decision on *Airtours/First Choice* Merger.[1]

Introduction.

Last week the EU Court of First Instance (CFI) overturned the EU Commission decision prohibiting a proposed merger between Air Tours and First Choice, two of the four main UK holiday tour operators.[1] This is the first time that the CFI has overturned a merger decision since the Merger Regulation was introduced in 1990. The CFI concluded that the Commission had *"prohibited the transaction without having proved to the requisite legal standard that the concentration would give rise to a collective dominant position of the three major tour operators, of such a kind as significantly to impede effective competition in the relevant market."*[2] The judgment raises some serious questions about EU merger control policy.

Competitive Effects of Mergers. Horizontal mergers, i.e., mergers between firms that are competing in the same market, give rise to two types of potential problems.

- Unilateral effects arise where a merger creates or strengthens a dominant position enabling the firm to raise price unilaterally. Competition law may be ineffective at preventing such 'monopoly pricing' once a dominant position has been established.
- Co-ordinated effects arise where a merger would facilitate collusion. For example, the decline in the number of competitors may make it easier to detect cheating and thereby ensure that the remaining firms adhere to a cartel arrangement, thus facilitating overt collusion. Alternatively, a merger may reduce the number of firms to the stage where each of those remaining are far more likely to recognise that they can gain by not competing with one another, thus facilitating tacit collusion.

The characteristics of the particular market involved will determine which of the two types of problem might arise. For example, in differentiated product markets co-ordinated effects are of much less importance than unilateral effects. Most merger control regimes throughout the world apply one of two substantive tests:

- The Dominance Test - which is the test under the Merger Regulation; or
- The Substantial Lessening of Competition Test - which is the test

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applied in the US and included in the Competition Act, 2002.

Arguably the dominance test is not particularly well suited to dealing with mergers involving co-ordinated effects.

Joint Dominance.

The Commission, in a number of decisions, has developed the concept of joint dominance as a basis for blocking mergers involving co-ordinated effects, i.e., increased risk of collusion. In *Nestle/Perrier*, for example, the Commission concluded *"that the incentive and possibility to increase prices jointly had already been recognised by the companies in the past and that the proposed concentration would facilitate and reinforce the likelihood of such a strategy."*[3]

The European Court of Justice confirmed the application of joint dominance in merger cases in *Kali* and *Salz* but stated that in order to establish joint dominance there was a strong onus of proof to show that the merged firm would act as a single entity with its competitors.[4]

The *Airtours* Judgment.

The CFI expressed strong criticism of the Commission decision which sought to extend the concept of joint dominance to encompass a merger that would reduce the number of major firms from four to three. It rejected Commission arguments that the merger would facilitate tacit collusion. In particular the CFI found that, in the event of the merger, firms would have insufficient information to detect 'cheating', i.e., firms deviating from the collusive outcome. It also found that there would be no credible deterrent that might discourage 'cheating' and thus provide firms with an incentive not to compete. Consequently, the CFI found that *"the Commission made errors of assessment when it concluded that if the transaction were to proceed, the three major tour operators remaining after the merger would have an incentive to cease competing with one another."*[5]

Possible Implications.

The Commission Green Paper reviewing the operation of the Merger Regulation, which was published last December, raised the question of whether the Regulation should be amended to incorporate the *"substantial lessening of competition test"*.[6]

The judgment deals with the evidence on coordinated effects at some length. The CFI ruled that the Commission had failed to show that tacit collusion was likely. It would appear from the judgment that the CFI overturned the decision because of shortcomings in the Commission's economic analysis. Thus, the judgment, of itself, would not appear to raise questions about the appropriateness of the substantive test contained in the Regulation.

Nevertheless, the Commission may find it difficult to block future mergers where collusion is a concern unless the substantive test is changed.

The CFI's criticisms of the Commission's economic analysis may increase concerns about a procedure whereby a Commission official contesting a proposed merger also acts as decision maker. The CFI stated that *"…the Decision, far from basing its prospective analysis on cogent evidence, is vitiated by a series of errors of*

assessment as to factors fundamental to any assessment of whether a collective dominant position might be created."[7] The case also highlights the lack of effective redress for parties in cases where the Commission is found to have erred. Although the appeal was successful, it is almost certainly too late for the merger to proceed.

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1 *Airtours plc v. Commission,* case T-342/99, judgment of 6 June 2002.
2 Para 294.
3 OJ 1992, L356/1.
4 *France v. Commission,* [1998] ECRI -1453.
5 Para 182.
6 *Green Paper on the review of Council Regulation (EEC) No. 4064/89,* Com(2001) 745/6 Final.
7 Para 294.