GUIDELINES ON THE ASSESSMENT OF NON-HORIZONTAL MERGERS AND ACQUISITIONS

1. INTRODUCTION

(1) Article 7 of the Act no 4054 on the Protection of Competition (Act no 4054) prohibits one or more undertakings from implementing merger or acquisition transactions with a view to create a dominant position, or strengthen their existing dominant position, which would result in significant lessening of competition in a market for goods or services within the whole or part of the country. "The Communiqué Concerning the Mergers and Acquisitions Calling for the Authorization of the Competition Board," numbered 2010/4, and article 7 of the Act no 4054 identify which mergers and acquisitions must be notified to the Competition Board and receive the authorization of the Board in order to become legally valid, and they also establish the procedures and principles related to the notification of these transactions.

(2) The concept of dominant position is defined in article 3 of the Act no 4054 as "the power of one or more undertakings in a particular market to determine economic parameters such as price, supply, the amount of production and distribution, by acting independently of their competitors and customers". Within this framework, certain initial assessments have to be made concerning whether, as a result of a merger or acquisition in a goods or services market, undertakings may, individually or jointly, acquire the power indicating a dominant position or strengthen that power.

(3) The purpose of these Guidelines is to lay down the general principles to be taken into consideration in the initial assessments to be conducted by the Competition Board (Board) in relation to non-horizontal mergers and acquisitions.

(4) In competition law, merger and acquisition transactions between undertakings operating in different relevant product markets are defined as *non-horizontal mergers and acquisitions*[1].

(5) In order to avoid repetition and ensure readability, in the following chapters of the Guidelines, the term "merger" shall be used to also cover the term "acquisition".

(6) Non-horizontal mergers generally include vertical mergers and conglomerate mergers.

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[1] In competition law, merger and acquisition transactions between undertakings operating in the same relevant product markets are defined as *horizontal mergers and acquisitions*.

(7) Vertical mergers refer to transactions implemented between undertakings operating at different levels of the supply chain. When assessing such transactions, markets in which the undertakings parties to the merger operate are generally distinguished as downstream and upstream markets. Undertakings active in the upstream market are assumed to provide input to the undertakings active downstream. For instance, in a merger between a cement manufacturer and a ready-mixed concrete producer, cement products will be considered to exist in the upstream market and ready-mixed concrete products in the downstream market, since cement is used as an input in ready-mixed concrete production. The input in question may be in the form of raw materials, semi-finished products and finished products, or it may be a particular type of service.

(8) Also, with respect to vertical commercial relationships, mergers between undertakings operating at the level of production, distribution and retail sales for a good or service will be assessed within the framework of vertical mergers, as well. In this case, in a merger between a producer undertaking and a distributor undertaking for instance, it will be assumed that the producer is operating in the upstream market while the distributor is operating in the downstream market. On the other hand, in case of a merger between a distributor and a retailer, the distributor will be considered to be in the upstream market, and the retailer in the downstream one.

(9) Conglomerate mergers are those implemented between undertakings with no horizontal or vertical relationships. In these Guidelines, it is intended to limit the scope of the assessments conducted in relation to conglomerate mergers to those mergers implemented between the providers of complementary products, products which are weak substitutes for each other, or products in the same series. For example, in the healthcare services market, mergers between hospitals providing services in different branches of medicine can be considered within this framework.

(10) These Guidelines generally include the points to be taken into consideration by the Board in evaluating non-horizontal mergers. The issues included in the Guidelines should not be perceived as being the result of a rigid approach replacing the approach of *examination of each case within the framework of its specific circumstances*, which is recognized as the general principle of competition law analysis; on the contrary, they should be viewed as headings to be evaluated as a part of the process for the examination of each case within the framework of its specific circumstances.

(11) Competition law and policy, in general, are built on the idea that effective competition is a process which leads to decreased costs and prices as well as to increased product quality and

consumer choice, and which encourages innovation. It is accepted that this process ultimately benefits consumers. Mergers which create dominant position in the market or strengthen an existing dominant position, pose the risk of significantly reducing competition and thereby depriving consumers of the benefits of competition. Accordingly, as a result of such mergers, one or more undertakings can profitably increase prices while reducing output, consumer choice, innovation and other benefits expected from competition[2]. Within this framework, Board supervision over mergers is intended to prevent consumers from being deprived of the benefits of competition in case undertakings significantly restrict competition by creating or strengthening a dominant position in the markets via mergers.

(12) When compared to horizontal mergers, non-horizontal mergers are generally less likely to significantly decrease competition by creating or strengthening a dominant position.

(13) Non-horizontal mergers, unlike horizontal mergers, do not lead to the direct elimination or reduction of competition between undertakings operating in the same relevant market. However, in some cases, undertakings in the upstream or downstream market may be significant potential competitors for each other.

(14) In vertical mergers as well as in certain conglomerate mergers, undertakings parties to the merger have complementary activities or products. The combination of complementary products or activities under the same economic entity may lead to significant efficiency gains. Such mergers are expected to provide benefits to consumers by the positive results to be attained from competition. Economics theory foresees that, as a result of vertical mergers between undertakings producing complementary products, monopolistic profit margins implemented in the upstream and downstream markets before the merger would be internalized post-merger. Elimination of double marginalization as a result of the merger will allow the vertically-integrated undertaking to profitably increase its production in the downstream market. In theory, it is known that the merger will incentivize the vertically-integrated undertaking to decrease its prices for the final product or increase its output, thereby increasing consumer benefits. Similarly, positive initiatives such as improving quality of service or innovation in order to increase sales at one level of the market will lead to some benefits with respect to the other level of the market, as well. Since a vertically-integrated undertaking would incorporate such benefits, it will have more incentives to take such initiatives.

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[2] In these guidelines, increased prices refer to all potential restrictive effects of mergers on competition. This concept also covers situations where prices decrease less, or are less likely to decrease, than they otherwise would have without the merger and where prices increase more, or are more likely to increase, than they otherwise would have without the merger.

(15) Moreover, vertical integration will decrease transaction costs while creating efficiencies with respect to the organization of the product design, production, sales and distribution processes.

(16) In addition, regardless of whether the products are complementary, mergers between providers of different products included in a series of products sold to the same consumer group may lead to certain other benefits to the consumers, such as providing them with one-stop shopping opportunities.

(17) On the other hand, however, in certain cases non-horizontal mergers can potentially create or strengthen a dominant position, and thereby can significantly lessen competition as a result.

(18) In these Guidelines, the concept of consumer includes intermediate consumers as well as final consumers. In case intermediate customers are actual or potential competitors of merging undertakings, the assessment is based on the effects of the merger on the customers to whom the merging undertaking and the competitors in question are selling. Accordingly, on its own, the fact that the merger would affect competitors at any level of the supply chain does not pose a problem. The important factor is the impact of the merger on effective competition. In particular, the fact that competitors would be harmed due to efficiency gains stemming from the merger does not cause competitive concerns on its own.

(19) Non-horizontal mergers have two types of negative effects on competition. These are *unilateral effects* and *coordinated effects*.

(20) *Unilateral effects* basically emerge when non-horizontal mergers may cause *foreclosure*. In these Guidelines, the concept of *foreclosure* refers to instances where actual or potential rivals' access to supplies or markets is hampered or eliminated as a result of the merger, thereby reducing these competitors' ability and/or incentive to compete. As a result of such foreclosure, the merged company and, possibly, some of its competitors may be able to profitably increase the

prices. A merger which leads to market foreclosure that may result in increasing prices shall be accepted to create a dominant position or strengthen an existing one and thereby significantly reduce competition.

(21) *Coordinated effects* refers to the case where undertakings which were operating without harmonizing their behavior before the merger, are significantly more likely, post-merger, to raise prices or reduce competition through coordination. In case undertakings in the market were already operating in coordination before the merger, a merger transaction realized in the

market will help maintain the existing coordination in an easier, more stable and more effective manner. It will be assumed that, as a result of a merger with coordinated effects, joint dominant position will be created or strengthened in the relevant markets, and thereby competition will be significantly reduced.

(22) When assessing the effects of the merger on competition, competitive conditions observed in the relevant markets before the merger are compared with the competitive conditions expected to develop following the merger. While the conditions at the time of the merger usually enables a relevant comparison, in certain cases certain changes projected to occur in the future in the relevant market are also taken into consideration. These assessments also take into account the likely entries and exits in the relevant market which are not related to the merger as well as the effects of regulations which will be put into force in the near future.

(23) In the assessment of non-horizontal mergers, positive effects stemming from the efficiencies caused by the merger should be factored in, together with the negative effects of the merger on competition.

(24) These Guidelines are comprised of the Introduction and the following chapters:

(a) Board's approach to market shares and concentration levels

(b) The effects of vertical mergers on competition

(c) The effects of conglomerate mergers on competition

2. MARKET SHARES AND CONCENTRATION LEVELS

(25) It may be accepted that non-horizontal mergers would have no negative effect on competition, unless the merged entity resulting from the non-horizontal merger transaction holds dominant position in at least one of the relevant markets in question after the merger.

(26) For assessments of dominant position conducted by the Board, market shares and concentration levels will be indicators providing important initial information concerning the market power of the merging undertakings and their competitors. In the next stage, the level of actual and potential competition in the relevant markets, barriers to entry, supply and demand trends, alternatives for undertakings to find providers and customers, their ability to access supply resources, etc. will be examined in light of the explanations to be given in the following chapters of the Guidelines.

(27) In case the value of the Herfindahl-Hirschman Index (HHI) is below 2500 in each relevant market and the market share of the merged undertaking in each market is below 25%, it may be assumed that the negative effects of the non-horizontal merger on competition are not at a level that would require a deeper examination and the prohibition of the merger. However, this assumption may not be valid if at least one of the following conditions are present:

(a) the merger involves an undertaking that is expected to expand significantly in the near future (due to a certain innovation, etc.),

(b) there are significant cross-shareholdings or cross-directorships among the undertakings operating in the market,

(c) one of the merging undertakings is likely to disrupt coordinated conduct in the market (the likelihood that it is a maverick undertaking)

(d) there are indications of past or ongoing coordination, or there are practices facilitating coordination.

(28) If, post-merger, the HHI level is below 2500 and the market share of the merged undertaking in each market is lower than 25%, this maybe a first indication that the merger in question does not lead to competitive concerns related to a reduction in competition. On the other hand, these thresholds are not legally binding and do not constitute a presumption. Hence, it was decided that it would not be appropriate for these Guidelines to include HHI and market share thresholds indicating levels for competitive concern.

3. VERTICAL MERGERS

(29) In the assessment of vertical mergers conducted by the Board, positive effects stemming from the efficiencies caused by the merger should be factored in, together with the negative effects of the merger on competition.

3.1. Unilateral Effects: Foreclosure

(30) A merger is said to cause foreclosure effects if actual or potential rivals' access to supplies or markets is eliminated as a result of the merger, thereby reducing these competitors' ability or incentive to compete. The factors that lead to foreclosure hamper market entries or the growth of existing players in the market in addition to create an exclusionary effect on the market. In order for foreclosure effects to be present, it is not strictly necessary that competitors are forced

to exit the market following the merger. It is sufficient for the merger to disadvantage the rivals and prevent them from competing effectively. As a result, market foreclosure effects are deemed to be anti-competitive in case merged undertakings and, possibly, some of their competitors are given the opportunity to profitably increase their prices following the transaction.

(31) Two types of *foreclosure* can be distinguished The first type of *foreclosure* is called *input foreclosure*. *Input foreclosure* may be defined as the merged undertaking restricting the access of its downstream rivals to important inputs they need, thereby raising their costs following the merger. The second type of foreclosure may be called *customer foreclosure*. Customer foreclosure refers to the merged undertaking restricting the access of its upstream rivals to a sufficient customer base following the merger.

(32) As well, vertical mergers may also lead to certain unilateral effects due to the fact that they provide access to critical commercial information to the merged undertaking concerning its competitors in the downstream and upstream markets. For instance, an undertaking which becomes a supplier for its downstream competitors post-merger can increase prices in the downstream markets based on the information it may acquire concerning its competitors. Similarly, the ability of the vertically-integrated undertaking to access critical information it holds may also prevent its competitors from entering the market or from extending it.

3.1.1. Input Foreclosure[3]

(33) Input foreclosure refers to a merged undertaking restricting supplies of the inputs it provides to its downstream competitors after the merger, thereby increasing the costs of its rivals by making it harder for them to procure inputs for prices and conditions similar to those before the merger. This would enable the merged undertaking to profitably raise the prices it charges to consumers. As mentioned above, for market foreclosure in the form of input foreclosure to lead to consumer harm, it is not strictly necessary for the rivals to be forced to exit the market after the merger. The benchmark in this assessment is whether increasing input costs would lead to higher prices charged to consumers. On the other hand, it is possible that efficiencies arising from the merger may provide opportunities or incentives to the merged undertaking to reduce prices, so that the overall effect on the consumer is neutral or positive.

[3] The concept of "input" is used as a general term to also cover access to infrastructure, intellectual property rights, etc.

(34) When assessing input foreclosure, the first factor to examine is whether the merged entity would have the ability to substantially foreclose access to inputs downstream. The second factor to consider is whether the merged undertaking would have the incentive to do so. Lastly, it must be taken into account whether a foreclosure to that end would significantly distort competition in the downstream market.

(35) In practice, these three benchmarks are often examined together since they are closely intertwined.

3.1.1.1. Ability to Foreclose Inputs

(36) Foreclosing markets via input foreclosure may occur in various forms. The merged undertaking may completely stop supplying input to its actual and potential competitors in the downstream market, limit the amount of input it supplies, increase its sales prices, or make conditions of supply less favorable than what they were before the merger. In addition, the merged undertaking may choose to employ a specific technology in its activities, which is not compatible with the production technologies of its competitors. Input foreclosure may also occur in less obvious forms, such as reducing the quality of the input supplied. When examining input foreclosures, the Board may take into account many likely alternative and complementary strategies.

(37) When assessing the likelihood of market foreclosure caused by input foreclosure, whether the input in question is an important one for the downstream product must also be taken into consideration. Foreclosure will only occur if the relevant input is important. An input may be deemed important because it is an important cost item for the downstream product, or because of other reasons unrelated to costs. For instance, production or efficient sales may not be possible in the downstream markets without the input concerned, or the input may be an important element of differentiation for the downstream product. In addition, the input may also be important because of high costs of switching to alternative inputs.

(38) The presence of foreclosure effects via input restriction, in other words, the merged undertaking having significant effect on the competitive conditions in the upstream market and on the price and supply conditions in the downstream markets, depends on whether the vertically-integrated undertaking formed after the merger holds a certain level of market power in the upstream market.

(39) In order to claim that the merged entity would have the ability to foreclose the market through input foreclosure, it must first be demonstrated that, as a result of foreclosing access to the input,

its availability in terms of price and quality in the overall downstream market would be negatively affected. The factors increasing the likelihood of this effect includes cases where independent input suppliers other than the merged undertaking have a relatively low level of efficiency, where they offer less desirable alternatives, where they are unable to expand input production in response to the reduction in input supply due to capacity constraints or due to decreasing returns to scale. In addition, the existence of exclusive agreements between the merged undertaking and independent input suppliers may also foreclose the access of downstream competitors to the input.

(40) When assessing the likelihood of foreclosure via input restriction, another possibility to consider is that the merged undertaking may, post-merger, stop its purchases from the independent input suppliers and procure the inputs it needs internally. In such a case, downstream rivals will be able to access the capacity on the part of the upstream independent input suppliers which is freed up from the merged undertaking. Thus, the effect of the merger will be limited to changing the purchasing patterns of its competitors in the downstream market, and access to input will not be foreclosed.

(41) The assessment concerning input foreclosure shall also take into consideration the possibility that competing undertakings may be able to implement certain counter-strategies in an efficient and timely manner. Striving to become less dependent on the input under examination by changing production methods or supporting the entry of a new supplier into the upstream market may be given as examples to the counter-strategies that may be employed by the competitors.

3.1.1.2. Incentives for Input Foreclosure

(42) The incentive (motivation) for input foreclosure depends on the degree to which this restriction would be profitable for the merged undertaking. Within this framework, when planning input foreclosure, the vertically-integrated undertaking should take into account the losses in profits it shall incur in the upstream market due to the reduction in input sales to actual and potential competitors. This loss in profits must be compared with the return to be gained, in the short or longer term, from the opportunity to increase sales in the downstream market or to increase prices charged to consumers.

(43) The vertically integrated undertaking shall take into account how providing input to its downstream competitors will affect the profits to be earned in both the upstream and the downstream markets. Other conditions constant, the lower the profit margins of the merged undertaking upstream, the lower the loss from foreclosing input. Similarly, the higher the

downstream margins of the merged undertaking, the higher the return from increasing market share downstream by foreclosing competitors.

(44) The incentive for the merged undertaking to raise downstream competitors' costs depends on the extent to which downstream demand is likely to be diverted away from excluded competitors towards the merged undertaking. This ratio will normally be higher where the capacity constraints of the merged undertaking are lower than non-foreclosed competitors or where the products of the merged undertaking are close substitutes for the products of foreclosed competitors. The effect of input foreclosure on the demand in the downstream market will be higher if the input concerned represents a critical component of the downstream products and if it comprises a significant portion of the cost for the downstream competitors[4].

(45) In addition, the incentive for input foreclosure also depends on the extent to which the merged undertaking can benefit from higher price levels downstream. The greater the market share of the merged undertaking downstream, the greater the amount of sales on which to charge increased profit margins, and therefore the greater the incentives for input foreclosure[5].

(46) If the merged undertaking is a monopoly in the upstream market, it may not have any incentive for input foreclosure following a merger, since it is already able to derive maximum profits in the downstream market. On the other hand, very high market shares does not always ensure maximum profits for the undertaking[6]. Such a conclusion would require a detailed analysis of the actual and future constraints under which the monopolist operates. An undertaking which

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[4] Conversely, if the input accounts for only a small share of the final product and is not of critical importance, the demand to be diverted to the merged undertaking may be negligible and even a high market share upstream may not give the undertaking the incentive for input foreclosure.

[5] The less chance the undertaking has to focus on a specific downstream market, the less incentive it will have to raise its prices for the input. This is because of the opportunity costs it would have to incur in other downstream markets. In this respect, in case the merged undertaking supplies input to more than one downstream markets or to ancillary markets, its likelihood for engaging in price discrimination may also be taken into account.

[6] For instance, the undertaking holding monopoly position, or a position approaching monopoly, may fail to derive maximum profits due to a so-called commitment problem. Commitment problem may be explained as follows: If, despite concluding an agreement with a single undertaking downstream to supply input at a high price on the condition that additional products are not sold to other buyers, the undertaking in the upstream market holding monopoly position, or a position approaching monopoly fails to comply with the agreement and increases the amount of input it supplies to the other undertakings in the downstream market, the agreement may become unprofitable for the former undertaking. Anticipation of this kind of opportunistic behavior by the undertakings downstream will prevent the undertaking holding monopoly position, or a position approaching monopoly, from deriving maximum profits from its market power. Vertical integration will provide the undertaking holding monopoly position, or a position approaching monopoly, with an incentive not to increase the sales to other undertakings in the downstream market in order to prevent likely losses in the downstream market (i.e. to commit). Another example where the undertaking holding monopoly position, or a position approaching monopoly will not be able to derive maximum profits is when it cannot differentiate its prices among customers.

cannot derive maximum profits despite holding a monopoly position in the upstream market may have incentives for input foreclosure following the merger.

(47) When assessing the incentives for input foreclosure, various considerations may also be taken into account such as the ownership structure of the merged entity[7], the strategies it implemented in the past[8], or internal strategic documents such as business plans. In case the merged undertaking engages in a specific conduct aimed at input foreclosure, the assessment concerning the input foreclosure must take into account the incentives behind the relevant conduct as well as the factors that would eliminate or reduce those incentives (such as whether the conduct is lawful).

3.1.1.3. Overall Effects on Competition

(48) Vertical mergers may allow the merged undertaking to increase the costs of downstream competitors. This would lead to an upward pressure on the competitors' prices, as well. The fact that a vertical merger includes such potential effects means that the merger in question may lead to market foreclosure. In order to conclude that a vertical merger creates or strengthens a dominant position, and thereby significantly lessens competition, the competitors who suffer increased costs must hold important roles in terms of competition in the downstream market and constitute a significant part of the market. Also, it is possible to accept that a competing undertaking with a relatively small market share compared to other undertakings may hold a significant competitive position in the downstream market because it is a close competitor of the merged undertaking or because it is distinguished by its competitive behavior.

(49) In addition, raising barriers to entry for potential competitors can also lead to the creation or strengthening of a dominant position, and thus to a significant lessening of competition. It is possible for a merged undertaking to refuse to supply input to potential downstream competitors or to supply input on less favorable terms than before to merger, which may create a barrier to entry for potential competitors and cause a strong deterrent effect on market entry. It may be said that effective competition in the downstream market is significantly impeded by raising barriers to entry, in particular if input foreclosure forces such potential competitors to enter both the downstream and the upstream markets in order to compete effectively in either market. The

[7] For instance, in case an undertaking managed under the joint control of two parties in the upstream market has only one party active in the downstream market, in light of the fact that the party that is not active downstream would not take into account the losses stemming from the input sales reduction in the downstream market, the merged undertaking would have relatively low incentives to foreclose access to the input.

[8] The fact that, in the past, a competitor with a similar market position as the merged undertaking has stopped supplying inputs may indicate that this strategy is commercially rational.

concerns related to raising entry barriers is particularly important with respect to those industries that are in the process of opening up to competition or are expected to do so in the close future[9].

(50) If the downstream competitors of the merged undertaking already have a vertically-integrated structure or if they are capable of switching to alternative input sources, this may prevent increases in the costs of these undertakings following the merger. Sufficient competitive pressure exerted by competing undertakings operating in this way may prevent the merged undertaking from raising prices.

(51) The effect of the vertical merger on competition in the downstream market must also be assessed in light of countervailing factors such as the presence of buyer power or the likelihood that potential market entries upstream would maintain effective competition.

(52) Further, when examining the effect of a vertical merger on competition, efficiencies stemming from the merger must be taken into consideration, as well. It may be concluded that, as a consequence of the efficiencies brought about by the merger, there are no grounds for prohibiting the merger. This requires providing evidence and explanations demonstrating that the efficiencies generated by the merger will provide the merged undertaking the ability and incentive to act for the benefit of consumers, thereby counteracting the likely adverse effects of the merger on competition.

(53) When assessing efficiency gains with respect to non-horizontal mergers, criteria included in Chapter 6 of the Guidelines on the Assessment of Horizontal Mergers and Acquisitions shall apply. For efficiency claims to be taken into account in the assessments, all of these conditions must be fulfilled: the merger must benefit consumers, it must be merger-specific and it must be verifiable.

(54) The following may be given as non-extensive examples to efficiency gains stemming from vertical mergers.

(55) In particular, two separate monopolistic profit margins established by both undertakings operating independently in the downstream and upstream markets before the merger will be internalized into the single undertaking formed post-merger. Depending on the market

[9] Care must be taken to ensure that regulatory efforts aimed at opening a market up to competition are not rendered ineffective through mergers between vertically-related incumbent undertakings.

conditions, elimination of double marginalization may allow the vertically-integrated undertaking to profitably expand production in the downstream market[10].

(56) A vertical merger allows the merging undertakings to better coordinate their production and distribution processes, and therefore to reduce inventory costs.

(57) Generally, vertical mergers may align the incentives of the parties to invest in new products, in new production processes and in the marketing processes. For instance, whereas before the merger, an independent distributor undertaking might have been reluctant to invest in advertising and informing customers about the quality the of products of the upstream undertaking (since such investment would also have benefited its competitors), the vertical merger may reduce such unwillingness.

3.1.2. Customer Foreclosure

(58) When an undertaking operating in the upstream market merges with an important downstream customer with significant market power, it is likely that competition may be prevented via customer foreclosure.

(59) Because the merged undertaking will also be active in the downstream market, it can foreclose access to a significant customer base to its actual or potential competitors in the upstream market, which may reduce the ability and incentive of its upstream rivals to compete. This may raise downstream competitors' costs by making it harder for them to obtain the input at the pre-merger prices and conditions. Thus, the merged undertaking can profitably raise its prices in the downstream market. On the other hand, efficiency gains resulting from the merger may lead the merged entity to reduce prices. For customer foreclosure to lead to consumer harm, it is not necessary that the merged undertaking's competitors are forced to exit the market. The relevant benchmark here is whether increasing input costs would lead to higher prices charged to consumers.

[10] It is important to recognize, however, that the problem of double marginalization is not always present pre-merger. For instance, there may already be a supply agreement between the parties to the merger, which includes a price mechanism providing for a pricing structure that eliminates double marginalization. In this case, the efficiencies associated with the elimination of double mark-ups may not always be merger specific since they can be achieved via vertical agreements which lead to less anti-competitive effects. In addition, the vertical merger may not fully eliminate double marginalization when there are capacity constraints with respect to input supply or when there is an equally profitable alternative use for the input. In such circumstances, the internal use of the input entails an opportunity cost. Using more of the input within the merged undertaking to increase production downstream can cause a reduction in the sales of the input in alternative markets. The incentive to use the input internally and increase output downstream would be higher when there is no opportunity cost.

(60) In an assessment of customer foreclosure, the first factor to examine is whether the merged undertaking would have the ability to foreclose downstream markets to its upstream competitors by reducing its purchases from them. The second factor is whether the merged undertaking would have the incentive to reduce its purchases from upstream competitors. Last factor to take into account is whether such a market foreclosure practice would have a negative effect on consumers in the downstream market.

3.1.2.1. Ability to Restrict Access to Downstream Markets

(61) A vertical merger may have negative effects on the upstream competitors by increasing their cost to access downstream customers or by restricting their access to a significant customer base. Customer foreclosure may take various forms. For instance, the downstream division of the merged undertaking may decide to source all of its input from its upstream division, thus stopping or reducing purchases from its upstream competitors, or it may start procuring input on terms which are less favorable to its competitors than those before the merger.

(62) When considering whether the merged undertaking would have the ability to foreclose the market by restricting customers, it must be examined whether there are sufficient alternatives in the downstream market for the actual or potential upstream competitors to sell their products. For customer foreclosure to be a competitive concern, the downstream division which is a party to the vertical merger in question must be an important customer and must hold significant power in the downstream market. Otherwise, if it is likely that a sufficiently large customer base may turn to independent suppliers, then a vertical merger of this kind is not expected to lead to competitive problems.

(63) Customer foreclosure can lead to higher input prices if there are significant economies of scale or scope in the input market or when demand is affected by network externalities. In such circumstances, upstream competitors' ability to compete can be impaired.

(64) For instance, customer foreclosure can lead to increased input prices when upstream competitors operate at or close to their minimum efficient scale. If input foreclosure and the corresponding loss of production increases the variable costs of the upstream competitors, this may result in an upward pressure on the input prices charged to the customers operating in the downstream market.

(65) In the presence of economies of scale or scope, customer foreclosure may also have negative effects on entry to upstream markets by reducing the profit forecasts of potential upstream competitors. Since customer foreclosure can have such deterrent effects on entry, input prices

may remain at a higher level as compared to the situation where customer foreclosure is non-existent, thereby raising the costs for the downstream competitors of the merged undertaking.

(66) Since customer foreclosure will have negative effects on the revenue streams of upstream competitors, it may lead to a loss of incentives for these undertakings to invest in cost savings, R&D and increasing product quality. This, in turn, carries the risk of reducing the competitors' ability to compete in the long run, and even causing their exit from the market.

(67) In assessments concerning customer foreclosure, the likelihood of the utilization of the input concerned in different markets must be taken into account. Upstream competitors subject to customer foreclosure may be able to maintain efficient production of the input in question in accordance with the demand in secondary markets or for other uses, without suffering significant increases in costs.

(68) The assessment concerning customer foreclosure shall also take into consideration the possibility that upstream rivals may be able to implement certain counter-strategies in an efficient and timely manner. Implementing aggressive pricing with a view to protecting sales levels in the downstream market in order to reduce the effects of market foreclosure may be given as an example to the counter-strategies that may be employed by the competitors.

3.1.2.2. Incentive to Foreclose Access to Downstream Markets

(69) The incentive for customer foreclosure depends on the degree to which this restriction would be profitable for the merged undertaking. Customer foreclosure can lead to price increases in the downstream and upstream markets, and can allow the merged undertaking to gain additional revenue. It has to compare these revenues with the costs it would incur because it will not be procuring input from its upstream competitors.

(70) If the upstream division of the merged undertaking is less efficient than the foreclosed suppliers, or if it is offering less attractive products due to product differentiation, or if it is operating under capacity constraints, then reducing purchases from its upstream competitors by customer foreclosure may lead to certain costs.

(71) When assessing the incentives for foreclosing access to downstream markets by customer restriction, the extent to which price increases stemming from customer foreclosure in the upstream and downstream markets would benefit the upstream and downstream divisions of the merged undertaking must be taken into account. In this context, in case the merged

undertaking has a relatively higher market share downstream, increased profit margins post-merger will ensure higher total revenues

(72) In case the merged undertaking engages in a specific conduct aimed at customer foreclosure, the assessment concerning customer foreclosure must take into account the incentives behind the relevant conduct as well as the factors that would eliminate or reduce those incentives (such as whether the conduct is lawful).

3.1.2.3. Overall Effects on Competition

(73) Foreclosing competitors in the upstream market via customer foreclosure may have adverse effects in terms of competition in the downstream market, as well. These effects may also harm consumers. If, as a result of a vertical merger, competitors upstream are denied access to a significant customer base in the downstream market under competitive conditions, the opportunity and ability of these competitors to compete in the foreseeable future may be reduced. Consequently, downstream competitors will be put at a competitive disadvantage, due to the raised input costs they will encounter. In turn, the merged undertaking can profitably raise its prices or reduce the overall output on the downstream market.

(74) The impact of customer foreclosure on consumers may take some time to materialize. Customer foreclosure will first cause a reduction in the revenues of upstream rivals. Consequently, various results may be expected, including a reduction of investments in increasing product quality, reducing costs, or reinforcing other competitive tools.

(75) In order to claim that a vertical merger shall create or strengthen a dominant position in an upstream market and thereby significantly reduce competition, it must be demonstrated that a significant fraction of total upstream output is affected by the merger in question. If there remain a number of undertakings in the upstream market that are not affected by the vertical merger, input prices and, consequently, prices in the downstream market may avoid rising due to the competitive pressure exerted by these undertakings. However, for the materialization of competitive pressure from such non-foreclosed competing undertakings, these undertakings must face no constraints (either capacity constraints or constraints related to product differentiation) for expansion.

(76) Competition in the upstream market may be significantly impeded by raising barriers to entry, as well. If, in order to compete effectively in the downstream or upstream market, a potential competitor must enter into both of the markets due to customer foreclosure, raising barriers to entry, particularly in the upstream market, may lead to the creation or strengthening of a

dominant position. In this context, customer foreclosure and input foreclosure may be part of the same strategy. The concerns related to raising entry barriers is particularly important with respect to those industries that are in the process of opening up to competition or are expected to do so in the close future[11].

(77) The effect of the vertical merger on competition in the upstream market must also be assessed in light of countervailing factors such as the presence of buyer power or the likelihood that potential market entries upstream or downstream would maintain effective competition.

(78) Further, when examining the effect of a vertical merger on competition, efficiencies stemming from the merger must be taken into consideration, as well.

3.2. Coordinated effects

(79) In general, mergers may set the ground for certain changes in the market behavior ıf undertakings. Undertakings that were operating without any anti-competitive agreements pre-merger may be more likely to conclude price agreements or otherwise coordinate their behavior on other anti-competitive matters following a merger in the market. As well, if certain undertakings were already coordinating their behavior in violation of the competitive process pre-merger, it may be claimed that a merger in the market may make the coordination in question easier, more stable and more efficient.

(80) Three conditions are necessary for coordination to be sustainable. First, the coordinating undertakings must be able to monitor each other to see whether the terms of coordination are being adhered to. Second, a deterrent mechanism needs to be established for those undertakings which intend to deviate from the coordination. Lastly, parties outside the coordination, including customers, must be unable to react in a way that would jeopardize the results expected from the coordination.

(81) Vertical mergers may serve as a factor which makes it easier for the undertakings in the upstream or downstream markets to reach an understanding on the terms of coordination.

[11] Care must be taken to ensure that regulatory efforts aimed at opening a market up to competition are not rendered ineffective through mergers between vertically-related incumbent undertakings.

(82) For instance, when a vertical merger leads to foreclosure, there will be a reduction in the number of effective competitors in the market. In general, a reduction in the number of the players in the market can make it easier for other undertakings remaining in the market to coordinate.

(83) Furthermore, vertical mergers may also serve to increase the symmetry between the undertakings operating in the market as well as market transparency. This may increase the likelihood of coordination between the undertakings in the market.

(84) Vertical mergers may also lead to the elimination of any maverick undertakings in a market. A maverick undertaking refers to those undertakings which, for its own benefit, refuses to coordinate with other undertakings and prefers aggressive competition. If the maverick is included in the vertical integration, the undertaking will no longer operate with competitive incentives. Thus, a further barrier before coordination will have been eliminated.

(85) Vertical mergers may facilitate the formation and maintenance of coordination by increasing the level of market transparency due to the fact that they allow the merged undertaking access to sensitive information on its competitors. This is because due to transparency, it would be easier to monitor and discipline deviations from the coordination. Where prices charged to final consumers are public while main input prices are confidential, in other words, where the downstream market is more transparent than the upstream market, coordination via vertical mergers will be more efficient. That is to say, vertical integration will give upstream undertakings the power to set final prices and monitor deviations more effectively.

(86) When vertical mergers lead to foreclosure, there may be a reduction in the number of competitors operating effectively in the market. This may make it easier for competitors to mutually monitor each other's conduct in the market.

(87) Vertical mergers may affect coordinating undertakings' incentives to adhere to the terms of coordination. For instance, a vertically-integrated undertaking may be able to effectively punish those undertakings deviating from the terms of coordination, if it is an important customer or supplier to them.

(88) Vertical mergers may reduce the likelihood of destabilization of the coordination by increasing barriers to enter the market or limiting the ability to compete on the part of those undertakings outside the coordination.

(89) In case there is an important buyer in the market, upstream undertakings may act to terminate an existing coordination in light of the benefits to be gained from making large sales to that buyer. However, the integration of such an important buyer with one of the competitors as a result of a vertical merger can increase the risk that coordination in the upstream market will be maintained.

4. CONGLOMERATE MERGERS

(90) Conglomerate mergers are mergers where the relationship between the merging undertakings is neither purely horizontal (being in the same relevant market) nor vertical (supplier-buyer relationship). In competition law practice, the focus is particularly on the positions held by the merging parties in closely related markets. Within that framework, the subject of the examinations are generally mergers involving markets which include complementary products and services, or activities belonging to a certain range of products or services that is generally purchased by the same customer group.

(91) In general, even though it is acknowledged that conglomerate mergers are not very likely to create or strengthen a dominant position, thereby significantly reducing competition, in certain situations this may be a possibility. In the assessment of conglomerate mergers, positive effects of such mergers including efficiency gains should be factored in, together with the negative effects of the merger on competition.

4.1. Unilateral Effects: Foreclosure

(92) Provision of related products and services by the same undertaking can grant the merged undertaking concerned the ability and incentive to use its strong position in one market as leverage in other markets by means of tying[12], bundling[13], or other exclusionary practices.

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[12] Tying may be defined as requiring the purchase of one good or service together with another good or service, in violation of business practices. Tying can be implemented by integrating what may be recognized as two separate products (technical tying) or through contracts (contractual tying). In tying practices, products sold together may have varying proportions within the bundle (e.g. printers and cartridges). Also, in tying, there may be instances where the tied products are offered for sale separately.

[13] Bundling practices may be examined under two categories: *pure bundling* and *mixed bundling*. In pure bundling, different products which are sold together are not sold offered for sale independently (e.g. it is not possible to buy stand-alone printers or cartridges). The proportion of the products within the bundle is fixed. In mixed bundling, on the other hand, different products within the bundle are also available separately; however, economically, it is more cost-effective to buy the products as a bundle than to buy them individually (e.g. buying the printer together with its cartridges is cheaper than buying a stand-alone printer and cartridge).

(93) Tying and bundling practices may reduce the ability and incentive of actual and potential rivals to compete. These negative effects may lead to a reduction in competitive pressure exerted over price increases by the merged undertaking.

4.1.1. Ability to foreclose

(94) As a result of conglomerate mergers, the merged undertaking may leverage its power in one market to foreclose competitors in another market via bundling or tying practices that use the different products sold by the undertaking. However, in order for these practices to be able to foreclose competitors, the merged undertaking must hold dominant position in one of the markets concerned. Bundling or tying can only cause substantial impact when at least one of the merging parties' products is viewed by customers as particularly important and when there are few alternatives for that product. The level of product differentiation in the market or capacity constraints are factors which affect the number of alternative products.

(95) Foreclosure will only be considered a potential concern if there is a large of customer base in total who tend to buy the products concerned individually. In case of an increase in the number of customers who tend to buy the products together instead of buying them individually, the demand for individual products bought separately will be affected more by bundling or tying. This effect will be higher if the products subject to bundling or tying are complementary products.

(96) Generally, the foreclosure effects of bundling and tying may be said to be more pronounced in markets where there are economies of scale or where the existing demand pattern has dynamic implications affecting the conditions of supply in the future. For instance, where an undertaking that supplies complementary goods and holds dominant position for one of these products (product A) engages in bundling or tying, a reduction may be observed in the sales of complementary products (product B) which are supplied by non-integrated suppliers. In cases where there are network externalities at play, bundling and tying will reduce the opportunities of competitors to expand their sales of product B. Besides, these practices may also have adverse effects on those competitors intending to enter certain complementary product markets. Potential entrants into the market may be negatively affected from fact that products of complementary nature with the product they intend to sell would be proportionately less available in the market.

(97) If the merged undertaking cannot turn their tying or bundling practices into a lasting strategy, the scope of the foreclosure effects of these practices would be decreased. Bundling or tying

practices with technical reasons may be accepted as longer lasting practices since their reversal would lead to certain costs.

(98) The assessment concerning conglomerate mergers shall also take into consideration the possibility that competing undertakings may be able to implement certain counter-strategies in an efficient and timely manner. For instance, it may be examined whether single-product undertakings may offer their products at more attractive terms in response to the bundling or tying strategy of the merged undertaking. Bundling and tying practices are less likely to lead to foreclosure effects if an undertaking is able to purchase the products offered in the market with bundling or tying, and profitably resell them separately. In addition, if competitors can adjust their pricing more aggressively to maintain market share, the foreclosure effects stemming from these practices would be mitigated.

(99) For cost-saving purposes, customers may prefer to buy all products they need from a single source (one-stop-shopping). In this respect, the fact that the merged undertaking will have a broad range of products does not mean that competition will be negatively affected under all circumstances.

4.1.2. Incentive to foreclose

(100) The incentive to foreclose the market through bundling or tying depends on the extent to which this strategy would be profitable for the merged undertaking. When making an assessment on this subject, a comparison must be conducted between the costs the merged undertaking would incur in order to implement these practices and the gains that would arise from the increase in the market share or prices within the markets concerned.

(101) *Pure bundling* and tying practices may entail losses for the merged undertaking itself. For instance, if a significant number of customers does not prefer the bundle, but instead chooses to buy only one of the bundled products, income from the sales of that product as contained in the bundle will fall. Furthermore, customers who, before the merger, used to combine a leveraging product of one of the merger parties with the products of other undertakings may stop using the product in question as a result of the pure bundling or tying practices implemented post-merger, or they may choose to buy the bundle in question from the competitors. Thus, the merged undertaking may suffer losses in the sales of this product.

(102) In this context, it would be relevant to compare the relative return for different products. It is unlikely that the merged undertaking would forego sales on a highly profitable market in order to gain market shares on another market where turnover and profits are relatively small.

(103) However, bundling and tying practices may also allow gaining market power, and thereby profits, in the tied product market, while protecting market power in the *tying product* market.

(104) When assessing the foreclosure incentives of the merged undertaking as a result of conglomerate mergers, the ownership structure of the merged entity, past strategies implemented in the market, or information included in internal documents such as business plans must be taken into account as well.

(105) For instance, where an undertaking operating in a specific market is jointly controlled by two undertakings only one of which is active in the neighboring markets, it may be expected that the party which is not active in the neighboring markets would not wish to forego the income generated in the market where they are jointly active.

(106) In case the merged undertaking engages in a specific conduct aimed at foreclosing the market within the scope of a conglomerate merger, the assessment concerning the conglomerate merger must take into account the incentives behind the relevant conduct as well as the factors that would eliminate or reduce those incentives (such as whether the conduct is lawful).

4.1.3. Overall impact on prices and choice

(107) Bundling or tying practices may result in a significant reduction of sales prospects faced by those competitors in the market which sell their products separately. Even though the reduction in sales by competitors does not, in and of itself, constitute a problem, if this reduction is significant enough in certain industries, in particular, it may lead to a reduction in competitors' ability or incentive to compete. This may allow the merged undertaking to gain market power in the market for the tied or bundled good, and to maintain market power in the market for the tying or leveraging good, which would lead to the acquisition of dominant position, or to the strengthening of an existing one.

(108) Practices aimed at foreclosure may deter entry by potential competitors in a specific market by reducing their future sales prospects in the market to a level below the minimum scale necessary for entry. In the case of complementary products, if potential competitors need to enter all complementary markets at the same time (rather than separately or sequentially) in order to compete effectively and if tying practices have deterring effects for one of the markets, then these practices would also lead to deterring effects in other complementary markets.

(109) When assessing the effects of foreclosure practices on competition, the first factor to consider is whether these practices affect a significant portion of the output in the market. In case, as a

result of a conglomerate merger, single-product competitors in any one of the markets concerned can compete effectively, it may be acknowledged that the merger in question is unlikely to create or strengthen a dominant position, and thereby to significantly reduce competition. It must also be taken into account whether these effective competitors have the ability and incentive to raise production.

(110) The effect of a conglomerate merger on competition in the markets must also be assessed in light of countervailing factors such as the presence of buyer power, or the likelihood that potential market entries downstream or upstream would maintain effective competition.

(111) Further, when examining the effect of a conglomerate merger on competition, efficiencies stemming from the merger must be taken into consideration, as well. Especially in case of complementary products, most of the efficiency gains defined in relation to vertical mergers would also apply to conglomerate mergers.

(112) For instance, undertakings which adjust the prices for complementary products independently would not take into consideration the positive effects of a reduction in the prices of one product over the demand for the other product. However, under certain market conditions, the merged undertaking can internalize this positive effect and act accordingly in case a decrease in the prices of one product leads to higher overall profits (Such practices are often referred to as the *Cournot* effect). It is observed that merged undertakings most often utilize this effect in *mixed bundling*.

(113) Conglomerate mergers may also provide cost savings in the form of economies of scope, both on the production and the consumption side. For instance, it may be more efficient to market certain products together as a bundle rather than separately. Moreover, supplying complementary components together may also result in consumer benefits in the form of component compatibility and quality assurance. Such advantages of economies of scope, however, are necessary but not sufficient requirements for the efficiency gains stemming from bundling or tying practices. Indeed, benefits from economies of scope frequently can be realized without any need for bundling.

4.2. Coordinated effects

(114) Conglomerate mergers, in some cases, may serve as a factor which makes it easier for the undertakings in the markets to reach an understanding on the terms of coordination. The observations and assessments of the Guidelines on the Assessment of Horizontal Mergers and Acquisitions concerning coordinated effects apply here, as well.

(115) A conglomerate merger may affect the possibility of coordination by causing a reduction in the number of effective competitors in a market. Moreover, even if rivals are not excluded from the market, these undertakings may become more vulnerable and, instead of contesting an existing coordination, may prefer instead to operate under the advantages provided by increased price levels.

(116) Conglomerate mergers may increase the extent and importance of the concept of multi-market competition. To wit, such mergers may be used as a mechanism to monitor the compliance of undertakings operating in more than one market with the coordination.