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CMA CLEARS VODAFONE/THREE UK MERGER: A LANDMARK DECISION – AND ITS IMPLICATIONS

The UK Competition and Markets Authority (**CMA**) has cleared the "four-to-three" mobile telecoms merger between Vodafone and Three. It did so on the basis of behavioural commitments by the merging parties to invest around £11 billion in their telecoms infrastructure, and to cap their prices temporarily, pending the realisation of the claimed pro-competitive effects of their investments.

The decision signals greater openness by the CMA to behavioural remedies instead of only structural divestments, as a basis for clearing mergers that raise some competition concerns. This may well create new business opportunities for M&A. It remains to be seen whether it will serve as an important precedent for consolidation in other sectors and countries, with the European Commission actively considering whether to soften competition policy for mergers.

Key issues

- How have competition authorities in Europe dealt with four-to-three telecoms mergers in the past?
- How does the CMA's decision differ from previous cases?
- Will the European Commission follow the same approach?
- What investment commitments were accepted by the CMA as a condition of clearance?
- What are the implications for other, future, mergers?

REVERSING THE TIDE

The CMA's decision signals the beginning of a reversal of two long-standing trends.

The first is the CMA's traditional preference, until now, that mergers that raise competition concerns should only be cleared if there are structural remedies, such as divestments, that can address its concerns. The CMA likes structural remedies because they avoid risks of unsuccessful design and implementation and do not need ongoing monitoring and ongoing compliance. The CMA's acceptance of behavioural remedies in *Vodafone/Three* signals a greater openness to non-structural remedies in the future. That this marks a change in approach rather than an isolated instance is illustrated by the recent announcement by the CMA's Chief Executive, Sarah Cardell, that the CMA is to conduct a broad review of its approach to remedies. This will consider when behavioural remedies may be appropriate, the scope for remedies that lock in genuine rivalry-enhancing efficiencies and the role for remedies to preserve relevant customer benefits which may offset anti-competitive effects.

The second trend which the *Vodafone/Three* decision challenges is the previous opposition of competition authorities in Europe to "four-to-three"

telecoms mergers between mobile network operators. The European Commission (**EC**) has asserted jurisdiction to review all previous major four-to-three mobile telecoms mergers in recent years, and has, with one exception,[1] consistently prohibited them, or cleared them on condition that the parties create a new fourth player. The most notable example is the EC's pre-Brexit prohibition of the merger between Three and O2 (now Virgin Media O2), a decision that was, at the time, supported by the CMA.

The CMA's decision to clear *Vodafone/Three* is the first indicator that this trend may be reversing. But it is not the only one. In the EU, a new Competition Commissioner, Teresa Ribera, assumed office on 2 December, with a mandate to revise the EC's guidelines for mergers between competitors to "give adequate weight to the European economy's more acute needs in respect of resilience, efficiency and innovation, the time horizons and investment intensity of competition in certain strategic sectors" (see our briefing for details). This mandate has been heavily influenced by a report of Mario Draghi, which argued that the EC should be more open to clearing mergers that are otherwise anticompetitive on the basis that they will increase innovation and that, as a condition of doing so, merging parties should be required to make binding commitments to make innovation investments. As explained below, the CMA's clearance of *Vodafone/Three* is conditional on such investment commitments.

These UK and EU developments suggest that the CMA's decision may be the precursor to a wave of consolidation in the European telecoms sector and, possibly, other sectors too.

THE CMA'S DECISION

Without the remedies, the merger would have been prohibited. The CMA predicted that it would have led to average price rises of 5.5% by Three and 2.6% by Vodafone. While the CMA accepted that the merger would create significant efficiencies that would lead to improved quality of services for customers and lower costs, these in themselves were not sufficient to offset the anticompetitive harm. In particular, the CMA considered that there was a significant risk that the parties' ambitious plans to invest £11 billion in their merged network infrastructure would be watered down, as applying alternative reasonable assumptions made the case for implementing them in full substantially less compelling.

It was this concern that the remedies addressed. The parties will have a binding commitment to implement their investment plan in full over an eight-year period. Changes to the law that become effective on 1 January 2025 will mean that the parties will have every incentive to comply: breaches of the commitments will result in potential fines for the merged entity of up to 5% of its group worldwide turnover, equating to maximum fines of around £4.2 billion on the basis of its parents' most recent consolidated financial statements.

The CMA found that, in comparison to a world without the merger, the commitments would lead to significantly greater:

- network capacity, in the form of more sites in which telecoms infrastructure would be deployed and more spectrum; and

[1] The unconditional clearance of the merger between T-Mobile and Tele2 in the Netherlands, on which Clifford Chance acted for Tele2.

- network quality, in the form of better coverage reliability, reduced congestion and greater availability of high-capacity spectrum coverage.

These effects were enhanced by a deal that the parties had agreed with one of their rivals, Virgin Media O2, to provide it with additional spectrum and greater access to the merged entity's sites for the deployment of its own telecoms infrastructure. Increased network capacity and quality would, in the CMA's view, drive sufficient competition between the remaining three market players to ensure that, in the longer term, there would be no price rises that would not have happened absent the merger.

However, the CMA concluded that these pro-competitive effects would grow over time as the investment and integration plan is implemented and that there would be a short-term period in which they would not offset the anticompetitive effects of the merger. The CMA therefore required the parties to also commit, for three years, to cap selected mobile tariffs and data plans and to offer pre-set prices and contract terms for wholesale services.

It is now for Vodafone and Three to offer final undertakings that will give effect to the remedies envisaged in the CMA's decision. Merging parties typically have up to 12 weeks to conclude this process (unless extended), which includes a public consultation on the proposed undertakings.

IMPLICATIONS FOR FUTURE MERGERS

As noted above, the signs for mobile and fixed telecoms-sector consolidation in other European countries are more positive than they have been for years. However, telecoms companies should expect competition authorities to be both cautious and rigorous in their approach to assessing the effectiveness and feasibility of investment remedies. The EC, for its part, has had its fingers burnt in the (albeit distant) past, when committed investments in electricity interconnection capacity between France and Spain failed to materialise.[2] It will therefore be watching closely for any problems or loopholes in the design and implementation of the *Vodafone/Three* remedies, which could inform whether the EC will follow the CMA's lead. However, similar remedies were accepted by the US Federal Communications Commission as a condition of clearance of the 2019 *T-Mobile/Sprint* merger. Now in their fifth year of implementation, annual progress reports indicate that those commitments have been complied with and have been effective in expanding the merged entity's nationwide and rural 5G coverage.

For mergers in other sectors, the CMA's clearance decision and its broader review of its approach to remedies indicate a shift to a more pragmatic approach to merger control in appropriate cases. Businesses contemplating M&A activity should have more scope to be imaginative and creative about remedies that might satisfy the CMA. Investment remedies of the type accepted in *Vodafone/Three* are likely to be appropriate in only a small number of cases, however, such as those with:

- substantial scope for merger-specific efficiencies. This is particularly pronounced in the telecoms sector, where combining merging parties' geographic coverage and rationalising duplicative infrastructure can result in large reductions in costs, both for existing infrastructure and new

[2] A condition of the EC's 2001 decision to clear Case No COMP/M.2684 - *EnBW / EDP / CAJASTUR / HIDROCANTÁBRICO*.

investments, that would not be achievable through cooperation arrangements such as network sharing agreements;

- rigorous monitoring and compliance mechanisms. A key factor in the CMA's assessment of the *Vodafone/Three* remedies was the presence of a sector regulator, Ofcom, with the expertise and resources to effectively monitor compliance; and
- willingness of the parties to accept the risk that future changes in market conditions make the committed investments less commercially viable.

These changes in approach of the CMA – and, potentially, the EC, given its new stated mandate – might not affect the great majority of mergers reviewed by those authorities, but in the right cases they could make a big difference, sparking waves of consolidation in certain sectors.

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