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Innovation Competition in EU Merger Control: The Commission in Pursuit of a New Greater Good?

Anne Robert (Sidley Austin LLP) · Tuesday, January 23rd, 2018

The European Commission's recent focus on the impact of mergers on innovation competition has sparked a heated debate amongst lawyers and economists. Innovation seems to have become the new "Greater Good" the Commission is pursuing when reviewing mergers, whether in the pharmaceutical or medical device sectors, in pesticides, engineering, ICT or other technology-driven industries.

The concept of innovation competition is, however, not new. The Horizontal Merger Guidelines include innovation as one of the parameters of competition to determine whether a transaction significantly impedes effective competition, and the guidelines state that a merger can eliminate an important competitive force when it combines two important innovators or eliminates a firm with promising pipeline products. The framework to assess potential innovation effects that may result from a non-horizontal merger is similar.

Beyond the merger context, the Horizontal Co-operation Guidelines list negative effects on innovation as a potential concern in R&D agreements between competitors. They distinguish between industries where the innovation process makes it possible to identify competing R&D poles at an early stage and industries where it is not possible to do so because innovation efforts are not clearly structured. The guidelines say that, in reviewing an R&D agreement involving one of the latter industries, the Commission will limit its assessment to existing product and/or technology markets and will consider the agreement's impact on innovation only in exceptional circumstances. The Technology Transfer Guidelines also state that it may be useful and necessary in a limited number of cases to analyze innovation competition where a licensing agreement affects innovation aimed at creating new products and where it is possible at an early stage to identify R&D poles.

In a recent pharmaceutical merger, the Commission raised concerns that the transaction would have impacted innovation competition because the acquirer would likely have ceased or delayed the development of its clinical trial program to prioritize the (slightly more advanced) trial program of the target. Both parties had overlapping clinical research programs developed for the treatment of different types of cancer, and the Commission found that the transaction would have brought together two of only three competing clinical research programs for the treatments concerned.

In another recent merger, the Commission assessed the merger's impact on what it called "innovation spaces" involving research on active ingredients that may potentially be used in multiple existing and/or future product markets. The Commission identified the parties' pipeline

products and lines of research and found that the transaction would likely have resulted in the delay, discontinuation or redirection of the parties' overlapping R&D lines and early pipeline products in such "spaces". According to the Commission, the merger would also have reduced the parties' incentives to discover and develop new active ingredients and would have reduced innovation competition in the industry as a whole.

Against that backdrop, the Commission's assessment of R&D programs and their impact on innovation competition raises important questions. Notably in the pharmaceutical sector, the Commission is now looking at therapies in early development phases, while it focused in the past on therapies at a late development stage. At an early stage, however, it is still highly uncertain whether development efforts will eventually be successful. This arguably makes an assessment of effects on innovation competition highly speculative. Although the Horizontal Merger Guidelines state that the Commission may in some circumstances take reasonably predictable future changes to the market into account, in the case of early-stage R&D what can reasonably be predicted is often limited.

The Commission's concept of "innovation spaces" requires parties to assess the possible impact of their transaction on innovation competition in a "space" rather than a defined product market. In spite of the Commission's extremely detailed analysis in the above-mentioned case, it remains unclear how such an assessment would work in practice. Similarly, it is unclear how the parties to a planned merger could assess, in advance, the likelihood that their transaction would result in an industry-wide impediment to innovation competition, especially in sectors where their competitors' new R&D projects and developments are well-kept secrets.

It also remains unclear to what extent the Commission is willing to take innovation-related efficiencies into account in its merger reviews and what types of efficiency arguments the parties will have to develop to show that their transaction will not harm innovation competition. Combining complementary R&D assets through a merger, for example, may lead to synergies enhancing the parties' ability and incentives to innovate, and, even in a highly concentrated market, the long-term effect of such enhancements may outweigh short-term negative effects such as price increases. Although the Commission has evaluated potential efficiencies in several cases, it has so far found them insufficient to outweigh the innovation concerns.

In the future, the Commission will hopefully limit its assessment of innovation competition to situations where it can clearly identify R&D poles and has compelling evidence that a reduction in innovation would cause competitive harm. With several mergers in R&D-intensive industries ongoing and surely more to come, the Commission may shed further light on its position. In the meantime, the debate about innovation competition is likely to remain a "hot" topic.

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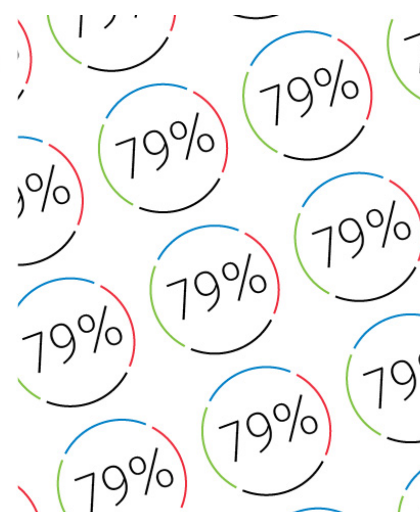

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