For more articles and information, visit
www.competitionpolicyinternational.com

H3G / Orange Austria – Mobile consolidation and Regulatory Reaction

Antonio Bavasso
Allen & Overy LLP
&
Dominic Long*
Allen & Overy LLP

*Antonio Bavasso is a Partner, Allen & Overy LLP; Visiting Professor at University College London, Co-founder and Executive Director of the Jevons Institute for Competition Law and Economics at University College London. Email: antonio.bavasso@allenovery.com; Dominic Long is a Senior Associate, Allen & Overy LLP. Email: dominic.long@allenovery.com. The authors advised Orange Austria and its controlling shareholder, Mid Europa Partners LLP, on the European merger control aspects of this transaction.

In this moth's Europe column, Antonio Bavasso and Dominic Long (Allen & Overy LLP) discuss the EU Commission's landmark clearance of the Orange Austria acquisition by H3G. The much-awaited decision came down last week, reaffirming the EC's traditional approach to merger control with a central focus on short to medium term price competition. This case marks the EC's first use of GUPPI methodology in a Phase II assessment of unilateral effects .The EC ultimately cleared the transaction subject to a package of commitments (including divestment of mobile telecoms spectrum) agreed after lengthy discussions between the parties, the EC and the Austrian national telecoms regulator, the TKK. In so doing, the EC has sent a strong signal that it will not wave through future consolidations in this sector on the strength of investment-related efficiency arguments alone: in announcing the EC's decision to clear the transaction, Vice President and Competition Commissioner Almunia cautioned "When consolidation takes place within the boundaries of an already concentrated national market, we should be careful about the potential harm to consumers...we do not have evidence that operators will invest more if they reach a bigger size, as long as markets will remain fragmented along national borders." We shall be waiting for the EC's published full decision to look for any hidden surprises.

Meanwhile, we hope you enjoy this month's Europe column!

On 12 December 2012 the European Commission (the **EC**) finally cleared the proposed acquisition by H3G Austria Holdings GmbH (**H3G**, a subsidiary of Hong Kong-based Hutchison Whampoa) of Orange Austria Telecommunication GmbH (**Orange Austria**) (the **Orange Austria Acquisition**).[1]

This acquisition came at a crucial phase for an industry that has been affected by an explosion in the use of data-intensive mobile devices and the related transitioning to the adoption of a new fourth generation technology of transmission (with Long Term Evolution or "LTE" rapidly emerging as the default 4G network standard for European operators). Regulators across Europe are engaged in designing or implementing auction policies to distribute 4G spectrum and maintain competitive structures in the market, mindful of the excesses of many 3G auctions in the nineties that left long lasting effects on the mobile telecoms sector.

At the same time, mobile network operators (**MNO**s) have stressed the need for greater consolidation to finance the up-front investments required to make that

[1] Case M.6497, *Hutchison 3G Austria / Orange Austria*, 12 December 2012.

transition. Some are calling into question regulatory policy that they believe to be excessively focused on a short term pricing dimension of competition and based on an unrealistic paradigm of perfect competition, which is not in line with the characteristics of this industry. The most vocal of those critics have gone as far as calling for a regulatory moratorium. Referring to continued regulation of wholesale interconnection rates and threats by the EC to cut European roaming charges, for example, Vittorio Colao, Vodafone's CEO, used a February 2012 keynote address to urge regulators to stop "*this continuous intervention on prices and let the industry reinvest the money*".[2]

Regulatory reaction to this line of reasoning has been mixed. The Commissioner charged with overseeing Europe's transition to next generation digital communication technologies, Neelie Kroes (who was previously European Commissioner for Competition), initially reacted very defensively. Speaking at the same conference, Commissioner Kroes made a point of noting that "*we need to promote sound and competitive markets…Competition has already delivered for the mobile user…From 2002 to 2010, mobile prices dropped 50 percent or more. Implementing the Commission's 2009 recommendation on mobile termination rates will take that even further: offering lower and fairer prices for virtually every European*."[3] However, Kroes has also hinted that there is an up side to cross-border consolidation: "*Having a few pan-European operators that are strong in the cross-border market would not necessarily be bad for competition,*" said Kroes, adding that **protecting consumers was about more than just ensuring a given number of operators in each country.** *"It can make sense ... and be good for investment and innovation*'" (emphasis added).[4] In clearing the Orange Austria acquisition, Joaquín Almunia, the present European Commissioner for Competition, echoed this sentiment but with an important caveat: "*I am aware that these new technologies require significant investments and – as you know – I will always support innovation. I think consolidation at E.U. level, especially across national borders, can be a good thing if it brings new services, more choice and lower prices to customers. However, we should also keep in mind that today, around 80 percent of mobile phone users in the E.U. are customers of the 4 biggest operators. So far, this cross-European parent ownership has not helped to develop*

---

[2] As reported on FT.com, 27 February 2012.
[3] See http://europa.eu/rapid/press-release_SPEECH-12-124_en.htm?locale=en.
[4] See http://uk.reuters.com/article/2012/06/11/us-media-tech-summit-kroes-idUKBRE85A12A20120611.

a Single Market where customers purchase or use their services freely across national borders."[5]

Against this backdrop, the Orange Austria Acquisition quickly became an important precedent for telecoms regulatory and competition policy. In the UK, the *T-Mobile/Orange JV*[6] case, which led to the creation of what is now known as EE, previously demonstrated how much interaction there can be between the EC, which as a guardian of European competition policy had to approve that joint venture, and national competition and regulatory authorities. In that case, which led to the reduction of U.K. mobile operators from 5 to 4, the national competition authority (the OFT) wanted to review the deal and therefore requested a referral back. The EC refused and the case was decided in Brussels. It was cleared subject to, *inter alia*, a spectrum divestment commitment which was devised in close co-operation with Ofcom (the UK's sectoral regulator).

However, the Orange Austria case involved a whole new level of jurisdictional interaction and overlapping reviews. The main acquisition was inter-conditional with a proposed on-sale by H3G to A1 Telekom Austria AG (A1) of Orange Austria's subsidiary, Yesss! Telekommunikation GmbH (**Yesss!**) (the **Yesss! Acquisition**), which fell outside the competition jurisdiction of the EC under the E.U. Merger Regulation (**EUMR**) and was therefore notified separately to the Austrian Bundeswettbewerbsbehörde (**BWB**). In addition, H3G agreed separately to sell certain spectrum and assets to A1 (the **A1 Spectrum and Assets Acquisition**). Both the transfer of spectrum from Orange Austria to H3G under the Orange Austria Acquisition, as well as the transfer of spectrum from H3G to A1 under the A1 Spectrum and Assets Acquisition, were subject to a review and approval under national legislation by the Austrian telecoms regulator, the Telekom-Control-Kommission (**TKK**). The overall transaction therefore involved two separate merger control approvals (EC and national) plus two separate national regulatory approvals.

As such, this would have been a perfect case to put into use European rules that allow national and EC merger control approvals to be co-ordinated with a system of referrals up from national authorities to the EC and down from the EC to national authorities. Ultimately, however, that system failed. The BWB asked for a referral back of the Orange Austria Acquisition (as the OFT did in *T-*

---

[5] European Commission press conference SPEECH/12/946, *Joaquín Almunia Vice President of the European Commission responsible for Competition Policy Introductory remarks on Hutchison 3G Austria/ Orange Austria merger decision*. Available at http://europa.eu/rapid/press-release_SPEECH-12-946_en.htm?locale=en.
[6] Case M.5650, *T-Mobile/ Orange*, 1 March 2010.

Mobile/Orange JV) under Article 9 of the EUMR. However, the EC, consistent with its decisional practice in this sector, did not accept that request which was eventually abandoned as the Orange Austria Acquisition went into Phase II.[7] The BWB for its part was equally unwilling to refer the Yesss! Acquisition up to the EC under Article 22 of the EUMR. As a result, there was no consolidation of the two competition reviews (let alone with the two separate national telecoms regulatory reviews), which proceeded in parallel relying on informal co-operation between the EC, the BWB (and subsequently the Austrian Cartel Court) and the TKK.

The Yesss! Acquisition was eventually approved after an in-depth review by the Austrian Cartel Court on 27 November 2012, although that decision can still be appealed before the Austrian Supreme Court. The following day the TKK published its draft approval of the spectrum transfer in the Orange Austria Acquisition. This was followed on 13 December 2012 by the TKK's formal clearance of the spectrum transfers in both the Orange Austria Acquisition and the Yesss! Acquisition.

The Commission defined – primarily by virtue of supply-side considerations – a single market for the provision of mobile telecommunications services to end customers in Austria. On this basis, although the Orange Austria Acquisition reduced the number of MNOs from 4 to 3, the merged entity would still have been the smallest operator in Austria with a market share in the low 20s behind A1 and T-Mobile. Pre-merger, there was only one mobile virtual network operator (**MVNO**) in Austria. Recital 32 of the EUMR states that concentrations giving rise to limited market shares may be presumed to be acceptable and a combined share below 25 percent is indicative of those situations. However, the Commission was keen to reject the idea that this creates an un-rebuttable presumption and assessed a number of sub-segments within this market: "*The economic analysis conducted by the Commission, taking into account the parties' particular strength in the private customer and data market segments, has shown that the market power of the merging parties would have been higher than what their market shares suggested*."[8]

The EC focused its analysis on possible unilateral effects particularly in certain sub-segments of the relevant market and risks that the elimination of Orange

[7] In the absence of a reminder from the BWB under Article 9(5) of the EUMR
[8] Commission Press Release IP/12/1361, *Mergers: Commission clears acquisition of Austrian mobile phone operator Orange by H3G, subject to conditions, 12 December 2012*. Available at http://europa.eu/rapid/press-release_IP-12-1361_en.htm.

Austria would have led to higher prices in the overall retail market for the provision of mobile telephony. In assessing those risks, the EC made use of a gross upward pricing pressure index (**GUPPI**). GUPPI is a metric used to evaluate a merger's potential for adverse unilateral effects in light of the expected post-transaction incentives of the merged entity to raise the price of one or more of the merging parties' products. It is a technique endorsed in the U.S. horizontal merger guidelines[9] and one that has been used in a number of previous OFT assessments of U.K. mergers. However, this is the first time the EC has used GUPPI in a Phase II assessment of a merger under the EUMR and the role of this type economic analysis in the context of the overall assessment is not well delineated.

The Commission ultimately dismissed the parties' arguments that the transaction would bolster the combined group's ability to roll out LTE. Interestingly, those investment-related efficiency claims were evaluated by the Commission against a hypothetical network-sharing counterfactual: "*we do not have evidence that operators will invest more if they reach a bigger size, as long as markets will remain fragmented along national borders…I can also think of other ways than mergers to promote efficiency gains among operators, such as network-sharing agreements*."[10] However, network-sharing arrangements of the type apparently favoured by the Commission as an alternative to mergers in this sector would still involve a reduction in competition at the network level, regardless of the legal and practical difficulties inherent in any agreement between competitors to collaborate at such a crucial stage of the supply chain.

Given the importance of the role of investment in transitioning to the new 4G technology, it is interesting to consider the spectrum position which would emerge post-transaction. Taking into account the transfer of spectrum from H3G to A1 under the A1 Spectrum and Assets Acquisition, post-transaction the three remaining MNOs would hold licences in each of the four different frequency bands that are currently available for mobile telecommunications in Austria:

Operator	900 MHz	1800 MHz	2100 MHz	2600 MHz
A1	2x20.2	2x15	2x19.8	2x25
T-Mobile	2x12.8	2x25.4	2x15	2x20
H3G	2x0.8	2x29	2x24.6	2x25

[9] US Department of Justice and Federal Trade Commission Horizontal Merger Guidelines, 19 August 2010.
[10] Speech by Vice President Joaquín Almunia, 12 December 2012.

Under the terms of Austrian MNOs' existing spectrum licences, frequencies in the 900 and 1800 MHz bands are currently assigned solely for the use of 2G (GSM) technology, while the 800 MHz band was historically used for broadcasting TV signals (i.e. not available to MNOs). However, following two recent decisions of the EC, a liberalisation of spectrum in the 800, 900 and 1800 MHz frequency bands is being rolled out across Europe, enabling that spectrum to be re-farmed for use with 3G (UMTS) and 4G (e.g. LTE) mobile telecommunications transmission networks.[11] In addition, a number of the Austrian MNOs' existing 2G licences are due to expire at the end of 2015 and 2017. As a result, the Orange Austria transactions took place in the context of an imminent auction by the TKK of a significant amount of mobile telecommunications spectrum in the 800, 900 and 1800 MHz frequency ranges.

The TKK therefore found itself in a unique position to influence the future parameters of competition in the Austrian mobile telecommunications market through: (i) setting the rules to be followed in the upcoming frequency auctions; (ii) stipulating conditions to its approval of spectrum transferred under both the Orange Austria Acquisition and the A1 Spectrum and Assets Acquisition; and (iii) the specialist advice it provided to the EC during its review of the Orange Austria Acquisition and to the BWB/Cartel Court in respect of the Yesss! Acquisition.
It is not surprising that the interaction between the TKK and the EC can be seen clearly in the final package of commitments accepted by the EC. In addition to a commitment to enter into a number of MVNO agreements (including at least one approved upfront) based on approved and published rates (which will guarantee the MVNO entry currently lacking in Austria) H3G also agreed to divest spectrum in the 2600 MHz frequency range (which is suitable for 4G services) to a new entrant that would also acquire certain spectrum in the 800 MHz range which, following a formal resolution of the TKK, will be reserved for this purpose in the upcoming auction.

This case demonstrates the important role national telecoms regulators can play in merger control assessments, both in terms of substance and in evaluating and advising on remedy packages. It also shows a substantial alignment between national telecoms regulatory policy (albeit under a EU regulatory framework) and EU merger control policy, and concurrence in the use of the regulatory tools.

[11] Commission decision of 16 October 2009 on the harmonisation of the 900 MHz and 1800 MHz frequency bands for terrestrial systems capable of providing pan-European electronic communications services in the Community (2009/766/EC), as amended by the Commission implementing decision of 18 April 2011 (2001/251/EU); and Commission decision of 6 May 2010 on harmonised technical conditions of use in the 790-862 MHz frequency band for terrestrial systems capable of providing electronic communications services in the European Union (2010/267/EU).

The EC was keen however to show that this case is approved without a revolutionary change in an analytical framework that remains firmly rooted in a traditional paradigm of short term consumer welfare which sets a very high threshold to factor into the analysis dynamic considerations of investment needs and incentives.