EU Merger Control

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Agenda

1. Introduction
2. The concept of concentrations
3. Substantive assessment
4. Procedure
5. Jurisdiction - referrals
6. Practical implications
General

- Purpose of merger control: Control with structural changes in the market
  • In contrast with antitrust rules: Anti-competitive behaviour prohibited
    - Anti-competitive agreements/concerted practices prohibited (Art. 101 TFEU/Art. 53 EEA)
    - Abuse of dominant position prohibited (Art. 102 TFEU/Art. 54 EEA)
  • Decisive: Change of control

- Compulsory pre-merger control/ex ante control
  • Analysis of potential effects on competition/Ex ante analysis
    - Comparison of the competitive conditions that would result from the merger with the conditions that would have prevailed without the merger
    - In contrast with the ex post control of Art. 101/102 TFEU (Art. 53/54 EEA)
  • Once and for all clearance

- Procedural characteristics
  • Compulsory notification
  • Stand-still obligation
  • Strict time limits for enforcement agency
Terminology: Concentrations between undertakings

- EU Merger Regulation: “Concentrations between undertakings”

- Types of concentrations
  - Mergers
  - Acquisitions
  - Joint ventures
Types of mergers

- Horizontal
- Vertical
- Conglomerate
Effects of mergers on competition

- Possible positive effects
  • Achieving economies of scale and cost reductions
  • Developing new products/markets
  • Promoting innovation and transfer of technology

- Possible negative effects
  • Strengthening of market power
  • Reinforcement of oligopolistic market structures
  • Raising/increasing of barriers to entry
EU merger control

- Supra national (EU) v. national rules
  - 2 sets of rules
    - The EU Merger Regulation
    - National merger control legislation
  - No overlap

- Scope of EU merger control
  - Concentrations with EU Dimension
  - The EU Merger Regulation (Reg. 139/2004), art. 1
  - Original and alternative turnover thresholds
The one-stop shop EU merger control

- Concentrations with EU dimension: National merger/competition law not applicable, art. 21(3)
  - Referral provisions: Re-attribution of cases between the Commission and the Member States
    - If EU dimension: From the Commission to Member States
      Cf. principle of subsidiarity
    - If no EU dimension: From Member States to the Commission

- Exception: Protection of Member States’ legitimate interests, art. 21(4)
  - Public security, plurality of the media and prudential rules shall be regarded as legitimate interests
EU Merger Control Authorities

- European Commission
  - DG Comp

- The General Court (previously the Court of First Instance)
  - Judicial review of European Commission’s decisions

- European Court of Justice
  - Appeals from the General Court

- No decentralised enforcement of EC Merger Regulation by National Competition Authorities
  - A case having a EU dimension may however be referred to the competent authorities of the Member States, cf. Article 4(4) and Article 9
  - If referral to Member States, national merger control legislation to be applied
Sources of law - overview

- The Merger Regulation (Reg. 139/2004)

- The Implementing Regulation 802/2004 (procedural rules; how to calculate time limits etc.)
  - Annex I: Form CO
  - Annex II: Short Form CO
  - Annex III: Form RS Reasoned Submission

- Judgments from the European Court of Justice and the General Court

- Decisions from the Commission

- Guidelines/notices from the Commission
Sources of law - European Commission’s Guidelines

- **Substantive issues**
  - Assessment of horizontal mergers (OJ 2004 C 31/5)
  - Assessment of non-horizontal mergers (OJ 2008 C 265/6)
  - Definition of the relevant market (OJ 1997 C 372/5)
  - Remedies acceptable (OJ 2008 C 267/1)
    - (See also Best Practices Guidelines)
  - Restrictions ancillary to concentrations (OJ 2005 C 56/24)

- **Procedural issues**
  - Consolidated Jurisdictional Notice (16 April 2008): Replaces former Notices
    - The concept of concentration (OJ 1998 C 66/5)
    - The concept of full-function joint ventures (OJ 1998 C 66/1)
    - The concept of undertakings concerned (OJ 1998 C 66/14)
  - Simplified procedures (OJ 2005 C 56/32)
  - Case referral (OJ 2005 C 56/02)

- **Best practices on merger control proceedings**
  - DG Comp Best Practices on the conduct of merger control proceedings (20 January 2004)
  - The Commission’s model texts for divestiture commitments and the trustee mandate (2 May 2003)
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Scope of EU merger control: Concentrations

- The concept of concentration: Change of control decisive element
  - Operations bringing about a lasting change in the control of the undertakings concerned, and therefore in the structure of the market
    - Internal restructuring within a group of companies are not included

- Types of concentrations, Article 3
  - Mergers
  - Acquisitions
  - Full-function joint ventures

- If no concentration, Article 101 TFEU may be applicable

- See also Consolidated Jurisdictional Notice, Part B
Acquisition of control - an overview

- Control
  - The possibility of exercising decisive influence on an undertaking
  - To determine its strategic commercial behaviour

- Types of control
  - Sole or joint control
  - De jure or de facto control
  - Direct or indirect control

- Ways of acquiring control
  - Acquisition of shares or assets
  - Acquisition of whole or part(s) of target undertaking
    - Legal entity, branches, assets
    - Must constitute a business to which a market turnover can be clearly attributed
Acquisitions of qualified minority interests

- **De facto control**
  - Likely to achieve a majority at shareholders’ meetings
    - Other shares widely dispersed
    - Evidence from the presence of shareholders in previous years

- **De jure control**
  - Specific rights attached to minority shareholding
    - E.g. preferential shares leading to a majority of the votes
  - Other rights/Shareholder agreements enabling the shareholder to determine the strategic behaviour of the target company
    - E.g. the power to appoint more than half the members of the Board

- **Options**
  - Will not in itself confer sole control; unless
    - Will be exercised in near future, and
    - Follows from legally binding agreement
Joint control

- Two or more undertakings/persons having the possibility of together exercising decisive influence over another undertaking
  
  - Decisive influence: Power to block actions which determine the strategic commercial behaviour of the undertaking
    - I.e. beyond veto rights normally conferred to minority shareholder

- Two parent companies each with 50 %

- Veto rights related to strategic decisions
  
  - In Statutes or shareholder agreements

- Elements in overall assessment
  
  - Appointment of management
  - Determination of budget
  - Business plan
  - Investments

- Strong common interests vs. shifting alliances
Creation of full-function joint ventures

- Three cumulative conditions for being subject to merger control
  
  • Joint control
    - Cf. previous slide
  
  • Full-function
    - Commission Consolidated Jurisdictional Notice
    - Performing all the functions of an autonomous economic entity
      Stability
      Dependence on parents
  
  • Lasting change in market structure
    - Entity created on a lasting basis
    - Financial resources
    - Personal resources

- If not subject to merger control; Article 101 TFEU may apply
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The SIEC-test

- Significantly impede effective competition, Article 2(2)
  - ”A concentration which would not significantly impede effective competition in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position, shall be declared compatible with the common market”
  - Causal link required between the concentration and effects
  - Market analysis
  - The SIEC-test replaced the Dominance-test

- Elements in the analysis
  - Definition of the relevant market
      - Product market
      - Geographic market
  - Competitive assessment:
    - General
      - Commission Guidelines on the assessment of horizontal mergers (2004 OJ C 31/03)
    - Theories of harm
    - Market power - Unilateral effects
    - Coordinated effects
    - Vertical effects
Definition of the relevant market

- Precondition for assessing possible restrictions on competition

- Purpose: To identify and define the boundaries of competition between companies
  - Identifying the products/services capable of constraining the behaviour of the parties to the concentration and preventing them from behaving independently of an effective competitive pressure

- Both a product and a geographic dimension

- Commission Notice on the Relevant Market
Significantly impede effective competition

- Horizontal effects: Unilateral effects
  - Creation or increase of market power
  - Ability to act independently of its competitors and customers
    - To profitably increase prices or reduce output, choice or quality
  - Merger with a potential competitor

- Horizontal effects: Coordinated effects
  - Collective dominance
  - Competitors more likely to coordinate their competitive behaviour?

- Vertical effects
  - Non-coordinated affects: Foreclosure
  - Coordinated effects

- Conglomerate mergers
Market shares and concentration levels

- Concentration levels
  - HHI (Herfindahl-Hirschman Index)
  - Adding the squares of the individual companies in the market
  - \( \Delta \text{HHI} = \text{Change in concentration as a result of the concentration} \)
  - Normally no horizontal competitive concerns if;
    - Post-merger HHI between 1000 -2000 and \( \Delta \text{HHI} < 250 \)
    - Post-merger HHI > 2000 and \( \Delta \text{HHI} < 150 \)

- Market shares as indication of unilateral effects
  - < 25 %: Presumed compatible
  - < 40 %: Normally no unilateral effects

- Market shares and concentration levels only elements in individual market analysis: Importance of countervailing factors
Sources of competitive constraints

- **Demand-side substitution**
  - Consumers’ response to a small but significant increase in prices
  - Depends on the reactions of the marginal consumers, not the average consumer
    - The issue is not whether all consumers react to an increase in prices by changing to another product but whether a sufficient number of consumers changes to other products or reduces their demand in an amount that makes the price increase unprofitable
  - The most immediate and effective disciplinary force, taken into account when defining the relevant market

- **Supply-side substitution**
  - Other suppliers’ ability to switch production to the relevant products
  - Shift must be possible in the short term and without incurring significant additional risks or costs
  - Taken into account when defining the relevant market

- **Potential competition**
  - Not taken into account when defining relevant market, but may be an effective competitive constraint
Possible countervailing factors

- **Possibility of market entry - Potential competition**
  - Entry must be likely, timely (2-3 years) and sufficient to deter any anti-competitive effects
  - Examples of entry barriers
    - Regulatory barriers
    - Technical advantages (e.g. preferential access to essential facilities or IPR)
    - Commercial and strategic barriers; Importance of brands, over-capacity, exclusive distribution networks and proprietary solutions
    - Importance of track records
    - Importance of economies of scale
    - Important sunk costs

- **Buying power**
  - Bargaining strength of the buyer vis-à-vis the seller in commercial negotiations
    - Depends on customer’s size, commercial significance and ability to resort to credible alternatives

- **Dynamics of the market**

- **Nature and structure of products and competition**
  - Differentiated or homogeneous products
  - Bidding markets
Efficiency defence

- Many mergers have both negative (anti-competitive) and positive effects
  - Positive effects e.g. efficiencies (economies of scale, economies of scope)
  - How should positive effects/efficiencies be balanced against negative effects in individual cases?

- Consumer welfare standard
  - Horizontal Guidelines, paras 76-88
  - A merger should not be prohibited if the efficiency gains are sufficiently substantial as to ensure that the price will not increase
  - Consumers should not be worse off as a result of the merger
  - Compare Article 101 TFEU
Failing firm defence

- Horizontal Guidelines, paras 89-91

- Failing firm
  - The allegedly failing firm would in the near future be forced out of the market because of financial difficulties if not taken over by another undertaking

- No alternative purchaser
  - There is no less anti-competitive alternative purchase than the notified merger

- Assets of failing firm will exit market
  - In absence of merger, the assets of the failing firm would inevitably exit the market

- “Burden of proof”
  - Notifying parties must demonstrate that the deterioration of competitive structure not caused by the merger
Ancillary restraints

- Ancillary restraints, cf. Article 6(1)(b) second subparagraph
  • Restrictions directly related to and necessary to the concentration
  • Automatically covered by a merger clearance
  • Principle of proportionality; restrictions on duration, geographical scope and products/services to be covered must be limited

- Commission Notice on ancillary restraints (OJ 2005 C 56/24)

- Example #1: Non-compete clauses on the seller
  • Purpose: To protect the value of the business(es) being transferred
  • Acceptable for 3 years when transfer of both goodwill and know-how
  • Acceptable for 2 years when only transfer of goodwill

- Example #2: Supply and purchase obligations
  • In order to maintain the continuity of supply in a transitional period
 Remedies

- Possible outcomes of investigation
  - Clearance
  - Prohibition

- Alternative outcome: Commitments by parties to overcome identified problems

- Types of remedies
  - Structural
  - Behavioural

- Notices
  - Notice on remedies, OJ 2008 C 267/1
  - Model text for Divestiture Commitments and Trustee Mandate, cf. Best Practice Guidelines

- DG Comp in-house Merger Remedy Study
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Concentrations with a EU dimension must be notified

- EU dimension defined by turnover thresholds only (regardless of effects on competition)

- Original thresholds, Article 1(2)
  - Combined global turnover: > EUR 5 billion
  - Individual turnover within EU of each of at least two undertakings concerned: > MEUR 250
  - Exception: 2/3-rule

- Alternative thresholds, Article 1(3)
  - Combined global turnover: > EUR 2,5 billion
  - Combined turnover within at least 3 EU states: > MEUR 100
  - Individual turnover of at least two undertakings concerned within the EU states: > MEUR 25
  - Individual turnover within EU of each of at least two undertakings concerned: > MEUR 100
  - Exception: 2/3-rule
Calculation of turnover (Art. 5)

- Starting point: Undertakings concerned
  - Undertakings participating in a concentration
  - Acquisition of parts of an undertaking

- The concept of turnover, Article 5(1)
  - Amounts derived from sales of products/services of ordinary activities last financial year

- Identification of undertakings whose turnover is taken into account, Article 5(4)

- Geographical allocation of turnover, Article 5(1)
  - Customer location

- The Commissions Consolidated Jurisdictional Notice, Part C
Who must notify and when to notify (Art. 4)

- Who must notify (Art. 4(2))
  - Mergers: The merging parties
  - Acquisition of control: The person(s) acquiring control
  - The seller has no obligation to notify

- When must notification be submitted (Art. 4(1))
  - “[P]rior to their implementation and following the conclusion of the agreement, the announcement of the public bid, or the acquisition of a controlling interest”
  - Notification may also be made where the undertakings demonstrate a good faith intention to conclude an agreement
The stand-still obligation (Art. 7)

- Purpose
  • To ensure the possibilities of effective merger control

- Automatic suspension
  • The concentration may not be put into effect/implemented until it has been cleared by the Commission
  • Legal exception: Public bids/series of transactions (art. 7 (2))
    - May be implemented, but no exercise of voting rights
  • Individual exemption: Derogation upon request (art. 7 (3))
    - Rarely granted

- Content
  • All implementing measures
    - Closing
    - Exercise of share-holders’ rights
    - Integration of the activities of the undertakings concerned
  • Preparatory measures may be taken
Timetable (Art. 10)

Pre-Notification

Stage I:
25 working days/
If commitments + 10
working days

Stage II:
90 working days/
If commitments + 15/20
working days

Notification CO

Art.6 (1)/(2) decision

Art.8 (1)/(2)/(3) decision
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One-stop shop principle

Alternative 1:
If EU dimension;
EU Merger Regulation -
The Commission
(MS’ legitimate interests)

The EU Merger Regulation: Turnover thresholds

Alternative 2:
No EU dimension;
National merger legislation -
National Competition Authorities

EU dimension: Referral from the Commission to Member States, Article 4(4) and Article 9

No EU dimension:
Referral from Member States to the Commission,
Article 4(5) and Article 22
Referral to Member States: Pre-notification by the parties (Art. 4(4))

- Test: Concentration may significantly affect competition in distinct market within a Member State

- Commission must be informed prior to notification by reasoned submission

- The Member State referred to in the RS must express disagreement or agreement within 15 working days of receiving the reasoned submission (silence = agreement)

- Commission may then decide to refer the whole or part of the case to the Member State
  • The case may even be referred to more than one Member State

- Commission’s decision must be taken within 25 working days after receiving the RS
Referral to Member States: Post-notification by Member States (Art. 9)

- A Member State may request referral within 15 working days after the case was notified to the Commission on its own initiative or upon the invitation of the Commission.

- Article 9(2)(a) test: Concentration threatens to affect significantly competition on a distinct market within a Member State.
  - Commission decides on the basis of the test but also has administrative discretion.

- Article 9(2)(b) test: Concentration affects competition on a distinct market within a Member State which is a non-substantial part of EEA.
  - Commission decides on the basis of the test, no administrative discretion (i.e. the Commission has an obligation to refer).

- Commission’s decision to refer or not shall as a general rule be taken within 25 working days from receiving the notification.

- The case may be referred as a whole or partially.

- The Member States shall inform undertakings of preliminary assessment within 45 working days after the Commission’s referral.
Referral to the European Commission: Pre-notification by the parties (Art. 4(5))

- Test: Concentration which is capable of being reviewed by at least three Member States
- Commission must be informed before any notification by reasoned submission
- Competent Member States must express disagreement within 15 working days of receiving the reasoned submission
- Member States’ veto: No referral where at least one Member State disagree
- If no disagreement, the concentration is deemed to have a EU dimension
Referral to the European Commission: Post-notification by Member States (Art. 22)

- One or more Member States may request referral within 15 working days after the case was notified.

- Test: Concentration affects trade between Member States and threatens to significantly affect competition within requesting Member States’ territory.

- Any other Member State shall have the right to join the initial request.

- National time limits suspended until Commission has made decision.

- Commission is deemed to have adopted decision to examine the concentration if no explicit decision within 10 working days after receiving the request.

- Commission examines the case on behalf of requesting Member State(s)
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Initial phase

- Feasibility studies
  - Buyer
    - Buyer’s assessment of regulatory risk: Will the concentration be prohibited/cleared on conditions/unconditionally cleared
    - If clearance on conditions - what conditions are likely (impact on price)
    - Alternatives to intended transaction structure
  - Seller
    - Seller’s assessment of regulatory risk (impact on price)

- Jurisdiction / notification
  - Notification to EU
    - Referrals to/from the Commission
  - Cross-border transactions: Screening of jurisdictions where notification may be required
  - Transaction structure may influence notification issues
Negotiation phase

- Handling of commercially sensitive information: Applicability of Article 101 TFEU
  - Information exchange between seller and buyer during negotiations
  - Due diligence

- Completion of due diligence - agreements in violation of Articles 101 and 102 TFEU
  - Article 101 TFEU: Cartel agreements - risk of sanctions
  - Article 101 TFEU : Other agreements - risk of invalidity
  - Article 102 TFEU : Risk of sanctions, invalidity, and profitability
  - Importance of compliance programs
Drafting of the sale purchase agreement

- Standstill obligation
  • Closing date
  • Long stop date
  • Independent until completion
    - Regulating the operation of the target company between signing and completion
    - Preparatory actions permitted

- Regulating regulatory risk, i.e. risk of intervention
  • Prohibition
  • Remedies
    - Structural
    - Behavioural

- The parties' rights and obligations in a regulatory process

- Ancillary restraints
  • Non-compete clauses
  • Licence agreements
  • Purchase and supply obligations