WHITE & CASE

# Global merger control: Crossing the finish line

In a period of economic, political and regulatory change, how can companies plot the right course for M&A success?

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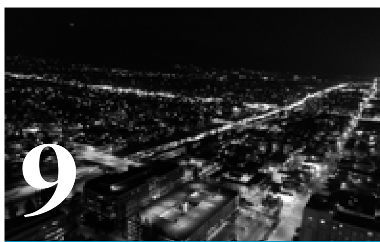


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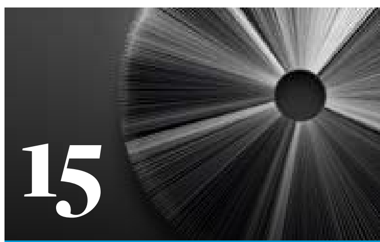


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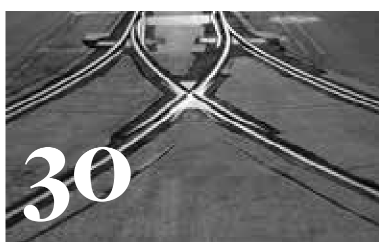


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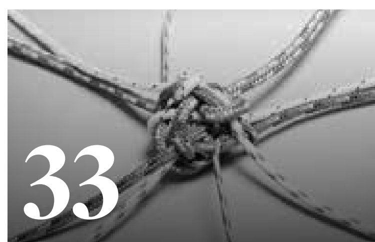


Too late for a fix?

# Merger control in a changing world

Global economic growth is back on the agenda and companies are once again looking to position themselves for success by pursuing mergers and acquisitions. But what are the prerequisites for success in an increasingly disrupted world?

*By J. Mark Gidley, Mark Powell*

Welcome to the second White & Case merger control publication, the first edition of which was warmly received. Earlier this year, it became apparent that an update was required, not so much driven by regulatory change, but rather to take into account policy shifts.

For example, we have seen the US catch up with Europe in relation to vertical mergers, the AT&T/Time Warner review being the most prominent recent example. At the same time, the European Commission has forged ahead again with a focus on conglomerate mergers and innovation markets. Perhaps the Dow/DuPont merger has attracted the most attention, as authorities now get out their telescopes and look far into the horizon to identify anti-competitive harm. There is a sense among the Commission's hard-liners that in the past too many mergers wriggled through without proper analysis. Our own view is that it may be legitimate to look ahead to try and identify harm (after all, that is what merger control is all about), but this long lens should not be forgotten when it comes to reviewing the synergies that a merger may create. However, Europe has set the tone, and we expect other authorities to follow.

Europe also seems to be taking the lead (and others will follow due to the prospect of publicity-garnering fines) in relation to procedural infringements. The argument for pursuing companies for inaccurate filings, for example, is that such violations call into question the very system of merger control. Be that as it may, due process needs to be followed in such cases, and this may divert valuable resources to past cases as opposed to dealing with the current case load. In other words, pursuing a few flagrant cases may be necessary to set a precedent, but they should not become regular items on the authorities' agendas (bringing with them attendant increases in filing times, and costs). Our view is that the authorities should confine their focus to statements that would have yielded a very different outcome, not mere technical infringements.

This leads us to the subject of gun-jumping. Again, viewed from afar, this should not be a problem in no-issues filings, and authorities typically have the tools to unwind a completed merger. The maxim 'no harm, no foul' ought to be applied to these cases to ensure that valuable resources are not frittered away on them.

In sum, our assessment is that the global system of merger control continues to limp along. However, the costs associated with a system containing myriad controls are increasingly high. Looking ahead, we wonder whether a fundamental overhaul is needed to ensure that transactions that pose no problems are not saddled with the costs imposed by the global system. (Yes, this will mean some authorities will have to relinquish jurisdiction in certain instances, safe in the knowledge that a transaction will be reviewed elsewhere.)

But more importantly, we continue to believe that the system of mandatory pre-merger review is fundamentally flawed and that instead we should shift to a system of voluntary merger control in which only mergers that present genuine issues need to be notified. Ironically, when commentators question whether the UK system of merger control needs to change in light of Brexit, one of the things that we would not change is the voluntary nature of the system.

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# Lenovo's merger strategy evolution

Lenovo's transformation from a national company into a global PC manufacturer has been underpinned by cross-border M&A that has allowed access to new markets and product segments. **Christophe Laurent**, EMEA General Counsel, discusses Lenovo's approach to global mergers

In just over a decade, Lenovo has expanded from a Chinese company into a diversified global manufacturer of PCs, servers, mobile phones and other electronic devices. This transformation has been driven by a number of cross-border acquisitions that have allowed Lenovo to quickly and efficiently enter new markets and product segments, notably with the purchases of the PC and server businesses of IBM, and the acquisition of Motorola.

**How would you describe your overall experience with antitrust authorities over the years?**
Merger control processes across the globe are becoming increasingly complex. In 2005, when Lenovo closed its first large acquisition—the purchase of IBM's PC business—the number of jurisdictions with active merger control processes was limited and the deal had only to be notified in a handful of jurisdictions. Less than ten years later, Lenovo had to notify its 2014 acquisitions of Motorola and IBM's server business in a much larger number of jurisdictions, some of which (like Ukraine) had very little apparent connection to the transaction. We were asked to understand and become familiar with regulatory regimes in South America or Africa, which had played a limited or even no role in global deals in the past. Moreover, over the past decade competition authorities have asked progressively more probing questions and investigations have become more inquisitive and detail-oriented. The remedies required are often complex and strategic decisions need to be made.

**As a General Counsel, what are your main merger control challenges?**
The main challenge is to keep the people involved focused on the deal. The business teams are busy with their day-to-day job and they often feel that once a deal is signed, they can move on to new goals and challenges. Antitrust merger control is not always their first priority. The General Counsel needs to keep them informed, explain why this is important and how the business can be affected if the antitrust review is not handled appropriately (for example, in terms of fines or delay in closing). In other words, my job is to educate the business people to respond to multiple requests for information in a very short period of time and help them understand the background behind the questions and what we want to achieve. This is one of the key challenges that needs to be addressed ever more efficiently in future transactions.

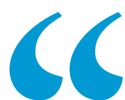
**What are some of the best and worst merger control experiences that you can share?**
Lenovo has had positive experiences with merger filings with the European Commission. All the deals that Lenovo has notified to the Commission were cleared in Phase I without commitments. However, merger notifications before other authorities were sometimes more challenging for Lenovo, primarily because of their unpredictability. In one case, regulatory approval took more than eight months. Such lengthy regulatory approvals create a lot of uncertainty, not just for our customers but also our employees.

**US$42.3bn**
Announced deal value in global computer sector in 2017

**Source:** Thomson Banker

**694**
Announced deal volume in global computer sector in 2017

**Source:** Thomson Banker



**Legal counsel is expected to be sufficiently flexible and creative in taking the specific aspects of each transaction into account and creating bespoke solutions**

**What are you looking for from your external counsel?**
Anticipation, planning and preparation. External counsel plays a crucial role in providing diligent planning of the merger control process, ensuring timely filings and fast clearances, which are crucial for any company. Lenovo seeks to avoid unnecessary delays, which have a real-life impact on the business, and expects its outside legal counsel to anticipate the most likely questions and information requests from the various authorities and prepare the legal team accordingly. This allows the company to focus its resources on collecting the required information—a complicated task for a global company like Lenovo, which has operations spanning a great number of different time zones across the globe.

We work with global law firms that can guide us through regulations in different jurisdictions and can ensure consistency of information and strategy across jurisdictions. Efficiency and avoiding duplication of work (which translates to lower legal fees) are very important for Lenovo.

Ultimately, every deal is different, and legal counsel is expected to be sufficiently flexible and creative in taking the specific aspects of each transaction into account and creating bespoke solutions that will allow the deal to close quickly and with as little trouble as possible. In this way, Lenovo can focus energy on its main goal—satisfying customers and shareholders.

**What are the recent trends for deals in the technology sector?**
For the past decade, we have observed increased consolidation in the technology sector. There used to be 25 PC vendors; now, we are down to five global players, with the top three PC vendors (Lenovo, HP and Dell) representing 60 per cent of the market.

Moreover, as large tech companies have expanded their reach into new product segments, some of Lenovo's suppliers and customers have become competitors. This changing landscape means that no merger notification in the tech sector is straightforward.

Technology companies are also looking at acquiring startups in related or unrelated technology markets, which has initiated some scrutiny under national rules, even if the merger thresholds are not met. In general, competition authorities seem to be focusing on the fast-developing technology world and mainly innovation. Is this a blessing or a curse? I guess time will tell.

**In 2005, when Lenovo closed its first acquisition, the deal had only to be notified in a handful of jurisdictions**

# Innovation in merger control

The European Commission is increasingly concerned that market consolidation will harm innovation and has changed dramatically the way it examines the impact of mergers on innovation. Merging parties should be prepared for it

*By Axel Schulz and Matteo Giangaspero, White & Case, and Benoît Durand, RBB Economics*

How the European Commission looks at the effect of horizontal mergers on innovation will be remembered as one of the important policy changes championed by European Commissioner Margrethe Vestager, who reminded the public that EU merger control rules 'are there to protect innovation', and that this objective 'is important in [our] merger policy'.

The Commissioner's public interventions have accompanied the rise of a novel theory of harm, which posits that horizontal mergers could 'lead to a reduction of innovation' in an industry as a whole. This was its position in relation to a merger between Dow and DuPont, where the Commission found the merger would significantly reduce innovation competition for pesticides. This theory led to the divestiture of DuPont's global R&D organisation in pesticides as part of the remedies required to clear the merger. In the recent Bayer/Monsanto merger, it seems that the Commission applied a similar approach, and found that the transaction would have 'significantly reduced competition in a number of markets' and 'significantly reduced innovation'. As part of the remedy package, Bayer has committed to divest three important lines of its global R&D organisation.

Although assessing the effects of mergers on innovation is not new—the Commission's Horizontal Merger Guidelines state that 'effective competition may be significantly impeded by a merger between two important innovators'—under Vestager's leadership the Commission's approach to the impact on innovation has changed dramatically.

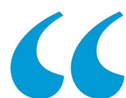
**Pipeline problems**

Traditionally, the Commission has examined whether a proposed merger creates an overlap between a product actively marketed by one of the parties with a pipeline product developed by the other party ('market-to-pipeline') or whether the parties developed separately pipeline products that would eventually compete on the market ('pipeline-to-pipeline'). Pipeline products include products at a relatively late stage of their development, with a good chance of launch within two to three years.

In the recent Pfizer/Hospira merger, the Commission found that the proposed transaction raised competition concerns because Pfizer was developing a competing medicine to Hospira's. Specifically, Hospira was selling Inflectra, an infliximab biosimilar used to treat several chronic inflammatory diseases, notably the inflammation of Crohn's disease. At the same time, Pfizer was in an advanced stage of developing its own biosimilar for infliximab. The Commission was concerned that Pfizer would likely discontinue its efforts to bring its new medicine to market, reducing competition. As a remedy, Pfizer divested its development programme.

In Johnson & Johnson/Actelion, the merging parties were separately developing new treatments for insomnia, using the same novel mechanism of action. The Commission was concerned that post-merger, J&J would have the ability and incentive to delay or abandon one of these programmes and thus required that Actelion's insomnia research programme be divested.

In the US, the Federal Trade Commission (FTC) has followed a similar approach. For example, in Thoratec/HeartWare, Thoratec was marketing a successful ventricular assist device (a heart pump) while HeartWare's device achieved promising clinical trials. The FTC



**R&D expenditures do not automatically translate into new products. Predicting the future isn't so easy after all**

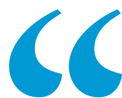
challenged the merger, alleging harm to innovation and to future price competition. In Nielsen/Arbitron, Nielsen offered a leading TV audience measurement service, while Arbitron offered a leading radio audience measurement service. At the time of the merger, both were developing a cross-platform audience measurement service. The FTC challenged the merger, alleging harm to innovation.

**Dramatic shift**

The Commission's approach in Dow/DuPont marks a dramatic shift in the way the impact of mergers on innovation is examined. The Commission did not focus on specific product overlap, as it did before, but instead it considered the impact on innovation 'as a whole'. Putting it simply, the Commission found that Dow and DuPont would likely reduce their R&D budget post-merger, which would inevitably lead to a smaller number of new products brought to the market.

But is it that simple? First, if the Commission found that a 'merger between important rival innovators is likely to lead to reduction of innovation', how is innovation measured? Surely by considering the launch of potential new products. But future new products (or products in an advanced-stage of development) were not the focus in Dow/DuPont. Can innovation be measured by R&D expenditures? Maybe. But R&D expenditures do not automatically translate into a guaranteed number of new products. R&D activities are a risky venture. Billions can be spent, often without immediate, or any, results. In the pharmaceutical industry, a recent study shows that only 9.6 per cent of drugs in Phase I are approved by the US FDA. The chance of success increases to 15.3 per cent in Phase II and 49.6 per cent in Phase III. Second, as the Commission puts it in its March 2017 decision (at 348), 'innovation should not be understood as a market in its own right, but as an input activity for both the upstream technology markets and the downstream [product] markets'. If that is the case and if the ultimate goal of merger control is to protect competition between 'downstream products', would it not be necessary that innovations worth protecting, although inherently uncertain, be at least to some extent identifiable with existing or pipeline products?

Third, merger control is inherently forward-looking and requires making predictions, which become increasingly imprecise the further into the future one looks. In past cases, that the competitive assessment focused on pipeline products seemed justified, in particular when it was expected that these products would hit the market in two to three years. Equally, merger-specific efficiency arguments are typically accepted within such a timeframe, so that they can be verified with at least some degree of predictability. In sharp contrast, between the moment new molecules are discovered and the point that firms can launch a new product, more than 10 to 12 years can pass. It is extremely difficult to make any sound predictions so far into the future.



**Parties should emphasise the complementarity of their R&D assets, which could lead to an increase in innovation**

Fourth, firms undertake R&D investments when they expect sufficiently high returns. Expected returns on such investments depend in part on the number of firms engaged in the same 'innovation space'. Obviously, the more firms that are involved, the lower the expected returns. Indeed, when a firm is the only one contemplating a research programme, it can expect greater reward than when others are pursuing the same research agenda. This means that a merger, by eliminating a rival, can increase the chance that the merged firm will undertake the necessary investment to pursue an ambitious R&D programme.

Finally, what can be an adequate remedy in such cases? Prohibit the merger as in Thoratec/HeartWare or Nielsen/Arbitron? In Dow/DuPont, in addition to product overlap divestitures, DuPont's pipeline in herbicides and insecticides, its discovery pipeline in fungicides and its entire R&D organisation had to be divested, including some 400 to 500 employees. Contrary to past cases, where pipeline products were sold to third parties, forcing the sale of an entire R&D organisation appears far more radical. But will such a type of remedy be successful? Will the R&D organisation be equally successful under its new owner? Will the scientists stay or leave for new ventures? Only time will tell. In the 1995 AMP/Wyeth merger, the parties divested one of the two development programmes for Rotavirus vaccines to the Korean Green Cross. More than ten years later, GSK launched a rival vaccine, while the Korean Green Cross never did. In Ciba-Geigy/Sandoz, the FTC was concerned that the merger could impair the development of gene therapy, a market that the FTC forecasted to be worth US$45 billion within 20 years from then. Although the parties divested one of the gene therapy programmes to Aventis, the market for gene therapy is still very small and Aventis has not launched a product in this space. Predicting the future isn't so easy after all.

**Business impact**

Clearly, the Commission's theory on innovation is here to stay. It seems to have applied it again in Bayer/Monsanto. Therefore, companies should consider carefully any overlap in innovation activities in a broad sense, even if there is no prospect of developing concrete products in the near future. Focusing on pipeline products is no longer enough to assess the regulatory risks posed by a transaction. Further, since the Commission's assessment relies heavily on internal documents, the parties should describe their R&D activities with care, highlighting the potential efficiencies of merging them. The parties should emphasise the complementarity of their R&D assets, which could lead to an increase in innovation. At the same time, highlighting the benefit of eliminating duplicative activities could backfire, as the Commission might interpret such a plan as a clear intent to reduce innovation competition. Finally, mergers that may be prone to the Commission's theory on innovation are likely to face an even longer pre-notification period.

# The devil's in the disclosure

Has the disclosure standard for companies been raised in the EU?

*By Strati Sakellariou-Witt*

In May 2017, the European Commission fined Facebook €110 million for providing incorrect information during the merger control process of its acquisition of WhatsApp. As per the Commission's statement, the magnitude of the fine was meant to send 'a clear signal to companies that they must comply with all aspects of EU merger rules, including the obligation to provide correct information'.

Then, in July 2017, the Commission opened two new investigations in relation to provision of incorrect or misleading information in the merger control context, and a number of national competition authorities fined companies for similar infringements. In short, this is a trend of which undertakings considering transactions should be mindful.

**Procedural obligations**

The obligation to provide accurate and complete information has been part of the European merger control rules since 1989. Between 1989 and 2004, however, the Commission brought only a handful of procedural infringement cases, and the fines were capped at just €50,000 per infringement.

In 2004, this threshold was significantly stepped up with the introduction of new merger control rules. Companies providing incorrect, misleading or incomplete information could be fined up to 1 per cent of their group's global turnover (the Commission also has the power to revoke a merger clearance decision).

Whereas procedural infringements in relation to antitrust investigations (which are also fined up to 1 per cent of a company's turnover) have been on the Commission's radar for some years now (in 2012, the Commission fined E.on €38 million for obstructing a dawn raid by tampering with the Commission's seal at E.on's premises), no procedural infringement cases under the new merger control rules had been brought for 13 years. Stakeholders were, thus, caught by surprise when a fine of €110 million was imposed on Facebook.

**€38m**

The amount paid by E.on in relation to procedural infringement in 2012

**Facebook in focus**

Facebook notified the Commission of its proposed acquisition of WhatsApp in August 2014 and received clearance two months later. At the time, Facebook had stated in its notification form that it would be unable to establish reliable automated matching between Facebook users' accounts and WhatsApp users' accounts. It repeated such information in a reply to a request for information from the Commission.

However, in August 2016, WhatsApp announced updates to its terms of service and privacy policy, including the possibility of linking WhatsApp users' phone numbers with Facebook users' identities. As a result, the Commission opened an investigation arguing that the technical possibility to automatically match Facebook and WhatsApp users' identities already existed in 2014, and that Facebook employees were aware of such a possibility.

Facebook acknowledged these facts and cooperated with the Commission by waiving a number of its procedural rights in order to close the matter swiftly. In exchange, its fine was reduced and it received a commitment that the final decision would mention that Facebook's conduct had only been 'at least negligent' (and not intentional) and the incorrect or misleading information provided by Facebook did not have any impact on the assessment carried out by the Commission in 2014. The Commission concluded that such acknowledgments were consistent with its own findings: The Commission had conducted an 'even if' assessment that assumed user matching as a possibility and had cleared the transaction nonetheless, and on balance, the evidence in the file supported a finding of 'at least negligence' rather than a positive finding of intent.

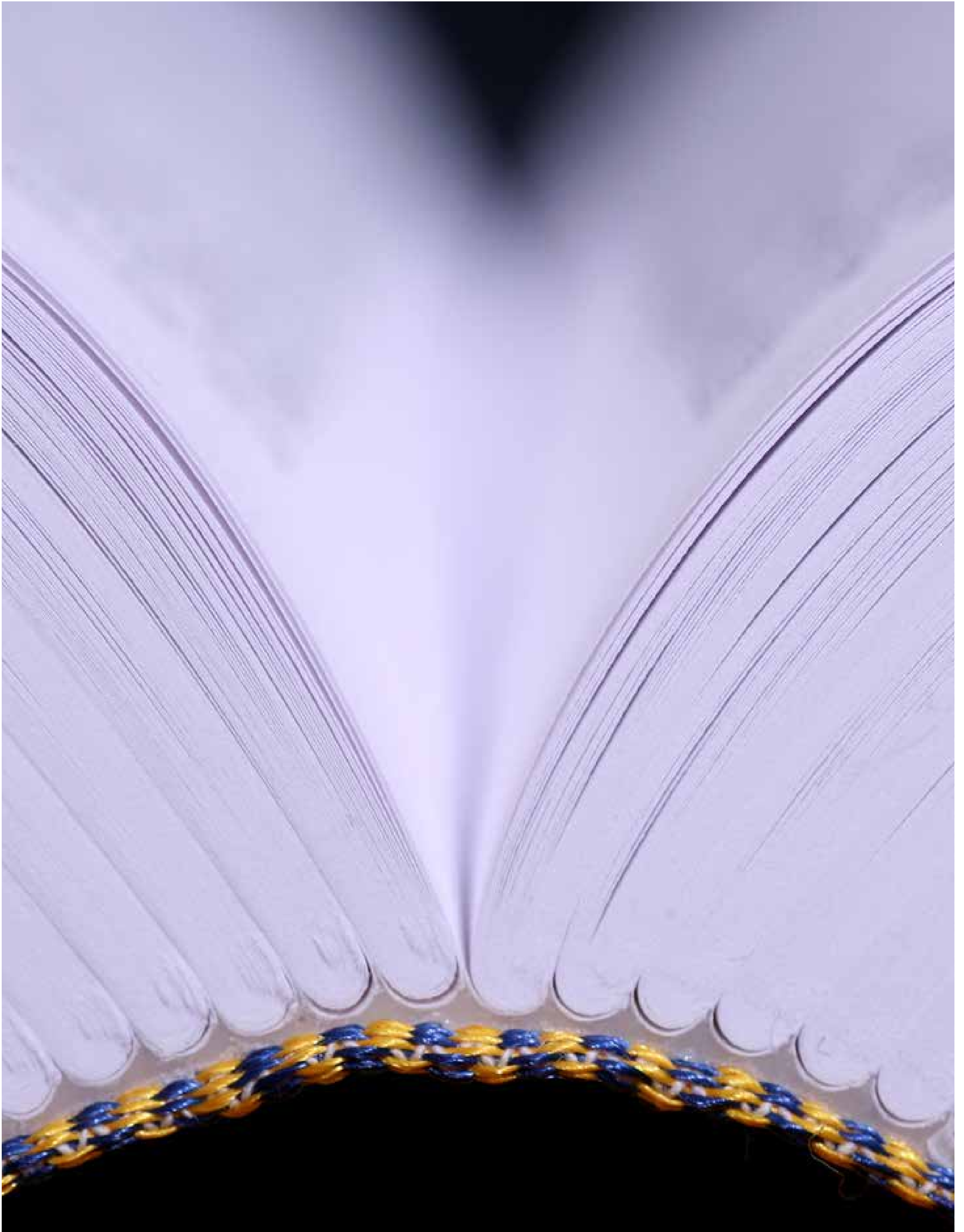
The Commission fined Facebook €55 million for the provision of false information in the notification form and a further €55 million for the provision of false information in the reply to the request for information.

The fact that the incorrect or misleading information had no impact on the outcome of the clearance decision and that Facebook had cooperated with the Commission were taken into account when assessing the gravity of Facebook's infringement. Ultimately, Facebook was fined on the basis of 0.2 per cent (as opposed to 1 per cent) of its global turnover (€28 billion). The Commission characterised the fine as 'proportionate and deterrent'.

**Cases in the pipeline**

Two months after the Facebook decision, on 6 July 2017, the Commission announced that it had opened investigations in relation to potential procedural infringements against Merck KGaA and General Electric.

The first case concerns a merger between two life-sciences companies,



Merck and Sigma-Aldrich, which was approved upon the condition of divestiture of part of Sigma-Aldrich's laboratory business. The allegation concerns provision of incorrect or misleading information, but no final decision has been reached.

The second case concerns LM Wind's acquisition by GE and centres on an alleged failure to provide information in relation to a company's innovation and R&D plans. The Commission argued that the omitted information had consequences not only for the Commission's assessment in the GE/LM Wind transaction, but also for a separate transaction in the wind turbine market (Siemens/Gamesa) that was being investigated at the same time. The information was allegedly necessary to assess GE's future position and the competitive landscape on the market in both cases.

GE withdrew its initial merger notification and re-notified the transaction, including the information on the R&D project that had not been included in the original notification. The re-notified transaction was cleared without commitments and no final decision in the infringement case has been reached.

**Ongoing trend**

In addition to these cases—which potentially expose businesses involved to fines of up to 1 per cent of turnover—the Commission opened two cases on gun-jumping (i.e., early implementation and integration of two merging companies in advance of obtaining Commission approval), Canon/Toshiba Medical Systems and Altice/PT Portugal. In such cases, companies can be fined up to 10 per cent of their turnover. On 24 April 2018, Altice was fined €125 million.

A number of European authorities have also initiated investigations at the national level on procedural infringements in the merger control context. On 2 May 2017, the Hungarian competition authority, after concluding, following an exchange with the US authorities, that data provided by Infineon were incorrect, revoked the Infineon/Wolfspeed merger clearance decision and imposed a fine of €242,000 on Infineon. Similarly, the Danish, UK and Polish authorities have imposed fines of between €6,000 and €23,000 on companies that allegedly failed to provide information during the merger control process.

**The Commission argued that the technical possibility to automatically match Facebook and WhatsApp users' identities existed in 2014, and that Facebook employees were aware of such a possibility**

**€242,000**

The fine imposed on Infineon after its clearance to merge with Wolfspeed was revoked

**Implications for companies**

The Facebook fine sent a strong signal to the business and legal community that the Commission will not shy away from imposing fines of tens of millions of euros if its procedural rules are infringed. To avoid hefty fines, companies will need to ensure that they provide accurate and complete information in the notification and divestiture process, including in the area of R&D and innovation, which can prove challenging. Indeed, in line with the Commission's current focus on the innovation effects of transactions (Dow/DuPont), the cases on misleading information concerned alleged omissions in relation to the companies' R&D projects.

In the future, when asked to provide all relevant information in the context of R&D, companies may face difficulties in identifying projects which are potentially relevant to the transaction.

A pipeline and R&D project that is not relevant for one market segment at the time of the notification can become relevant for that market in the future. Equally, a project that is immaterial at the time of the investigation can gain prominence later on. This means that counsel in merger control proceedings will need to have a full understanding of the potential relevance of R&D projects for the transaction and engage in discussions with the business teams (and, potentially the Commission early on in the process). This could result in an extension of the already lengthy pre-notification discussions.

Another difficulty is that if the R&D project lies with the target, the notifying party—which is responsible for the notification—will not be able to assess the relevance of the project, given gun-jumping rules that are in place and which primarily apply to competitively sensitive information such as R&D. This could result in companies amending the merger agreements by raising the disclosure standard.

Overall, there is a risk that, out of an abundance of caution, parties will submit relevant and non-relevant information to the Commission (and an enormous number of internal documents) in order to ensure that their notifications are complete and correct. This will increase the time and resources necessary on both sides. It could also make the conclusion of merger control proceedings difficult within the prescribed timeframes without repeatedly stopping the clock and thus, effectively, extending the time required to obtain EU merger control clearance. The right balance therefore needs to be struck between respecting the parties' procedural obligations and ensuring efficient merger control review.

# Mergers and the digital economy

When it comes to mergers within the digital landscape, the greatest challenge for regulation is to strike the right balance as regards enforcement. How are EU authorities taking action and what does this mean for the innovation economy?

*By Justus Herrlinger*

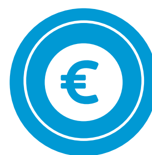
Rapid growth and change in the global technology sector and the evolution of digital economies have created new challenges for competition authorities. To keep pace with developments, the European Commission conducted a so-called sector inquiry in the field of e-commerce and published its findings in 2017. Currently, the EU is holding far-reaching discussions that could lead to the possible regulation of internet platforms and form part of a broader EU strategy for a digital single market.

National authorities are also starting to take action. Over the past five years, the German Federal Cartel Office (FCO —Bundeskartellamt), the main body responsible for German merger control rules, has made various interventions against agreements and practices in the online distribution field. In particular, the question of how to treat bans on sales via third-party internet platforms in selective distribution systems has been on the FCO's agenda for some time. In 2015, the FCO concluded that ASICS Deutschland had restricted online sales of running shoes in an anti-competitive manner.

The FCO has also launched an investigation into discrimination by retailers against online sales compared with offline sales. In June 2017, the FCO was handed additional investigative powers covering consumer protection, under which it has already launched a sector inquiry into online price comparison websites.

Another important aspect of competition law in the technology sector is merger control. Probably one of the most frequently discussed cases has been the US$19 billion acquisition of WhatsApp by Facebook in 2014. Despite the deal's large value and the fact that WhatsApp was already widely used in Europe, the transaction did not meet the turnover thresholds of any merger control regime in the EU. Politicians and competition authorities in Europe therefore discussed additional instruments in order to review and control these market developments. As early movers, Austria and Germany amended their competition laws in order to react to such new developments in the digital economy.

Among the changes, it has been clarified that services that are rendered free of charge to consumers may nevertheless constitute a market in terms of competition law. This is particularly relevant for multilateral online platforms such as search engines, comparison websites, hotel booking portals or social networks, which offer their services for no fee.



**€400m**

Under new laws, merger control will be required if the value of the consideration for a transaction exceeds €400 million in Germany (€200 million in Austria) even if the companies involved do not meet the domestic revenue thresholds

**Market power**

Another interesting aspect is the criteria for the assessment of the market power of companies on platform markets. The new law in Germany introduces specific criteria to be taken into account, such as: direct and indirect network effects; parallel use of multiple services and switching costs for users; economies of scale in the context of network effects; access to competitively sensitive data; and innovation-driven competitive pressure. These criteria or some of them have been applied before by other competition authorities. These legislative developments also prove that online markets constitute a special focus of competition law. To be appropriately applied, regulation in this field requires a thorough analysis beyond market shares and demand-side substitutability.

**US$19bn**

The acquisition of WhatsApp by Facebook in 2014, fell below EU merger control thresholds despite its hefty price tag

**New threshold**

The new laws on merger control take into account that many companies in the digital economy, especially when they are new, may offer their services without generating significant revenues but become relevant when other considerations such as personal data are taken into account. However, investors are ready to pay high prices for successful or promising digital companies. Thus, amendments include an additional merger-filing threshold based on the transaction value.

Under the new laws, merger control will also be required if the value of the consideration for the transaction exceeds €400 million in Germany and €200 million in Austria, even if the companies involved do not meet the domestic revenue thresholds. The consideration includes all assets and other monetary values or services the seller receives from the acquirer in the context of the transaction (purchase price) as well as the value of any obligations to be taken over by the acquirer. Furthermore, the target company must have significant

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**Online markets constitute a special focus of competition law. To be appropriately applied, regulation requires a thorough analysis beyond market shares and demand-side substitutability**

domestic operations. More jurisdictions are likely to follow in implementing these kinds of merger tests.

Given the dynamics of the technology and internet markets, one of the key challenges for competition regulation is to properly control M&A transactions without distorting incentives for competition for potential startups. From a company's perspective, merger control means additional bureaucratic hurdles, increased costs and time-consuming legal tasks. Hence, during the legislative discussions in Germany, startup companies raised concerns that an extensive merger control that included a standstill obligation until clearance may create a competitive disadvantage compared with other jurisdictions in the EU. As a result, investors might be deterred from investing in Germany. Against this background, the German national association of startups called for a European solution instead—this initiative could, however, not avoid the legislative changes.

**Care needed**

The challenge is to strike the right balance between potential over-enforcement and laxity. Predictions and projections on market development are particularly hard to make in this field. Even if a transaction falls under a broader value-based filing test, competition authorities must be careful in determining potential threats to competitors. A premature conclusion might, in fact, preclude a competitive offer to the market.

Instead of regulatory intervention, competition itself might sometimes be the solution. The next challenge for current incumbents might be waiting in the 'incubator', ready to be released for the next innovative, if not disruptive, service that will quickly change the current market shape—and welcoming competition as a discovery process.

# The EU approach to conglomerate effects

An increase in cases has been seen as a warning that the EU is ramping up its response to potential conglomerate effects. What can merging companies do to prepare for a challenge?

*By Strati Sakellariou-Witt, Jan Jeram*

In the aftermath of the attempted merger of General Electric and Honeywell in 2001—the first time that a proposed tie-up between two US companies had been blocked solely by European regulators—merger agencies in the EU and the US have adopted a consistent approach for global mergers and cooperate closely based on best practice guidelines. However, the approach on the two sides of the Atlantic remains inconsistent when it comes to assessing mergers that could have 'conglomerate effects'. These are transactions in which the parties are not competitors in the same product markets (there are no horizontal overlaps) and do not have a supplier-customer relationship (there are no vertical overlaps), but are active in two closely related (or neighbouring) markets. In such cases, the question is whether the merged company could leverage its power in one market over a neighbouring one, and exclude competitors in that second market.

**EU trend**

After prohibiting the GE/Honeywell and Tetra Laval/Sidel mergers in the early 2000s, mainly due to conglomerate issues and after being overruled by the European courts, the European Commission went quiet on conglomerate effects for more than ten years. In 2008, in its guidelines on the assessment of non-horizontal mergers, it stated that: 'Conglomerate mergers in the majority of circumstances will not lead to any competition problems' (at 92). However, recent decisions and pending cases reveal an increased pursuit of conglomerate cases. In 2016, the Commission examined four deals in close succession for potential conglomerate effects: Dentsply/Sirona (dental equipment and consumables); Worldline/Equens/Paysquare (payment software and relevant machines); Microsoft/LinkedIn (computer operating systems and social networking services/app) and Broadcom/Brocade (computer processors and interface cards). While in the US most transactions received unconditional clearances, the EU requested remedies from the parties in each one of these deals.

This trend continued in 2017 with the review of Qualcomm/NXP (baseband chips and near-field communication and secure elements chips), Essilor/Luxottica (eyewear and ophthalmic lenses) and Bayer/Monsanto (pesticides and seeds), all of which were subject to an in-depth investigation in the EU (varying from six to nine months), in addition to a (presumably) long pre-notification phase. By contrast, the Qualcomm/NXP deal was cleared in one month by the US authorities, and although the review of the Essilor/Luxottica transaction took longer, it primarily focused on raising rivals' costs and not bundling concerns.

**Concerns and remedies**

The main concern in conglomerates cases is whether the merged company will have the ability and incentive to foreclose rivals either by: a) tying products technically and degrading interoperability between the merged entity's products and competing products in favour of the merged entity's own downstream product; or b) bundling products commercially.

With the exception of Essilor/Luxottica and Bayer/Monsanto, in all cases examined and cleared by the EU, remedies were requested to address the conglomerate concerns (see panel opposite). These were mostly behavioural remedies—in the form of assurances that the parties will not eliminate competition—as opposed to structural remedies, which are preferred in cases of horizontal effects.

**Lessons learned**

While Commissioner Vestager maintains that the conglomerate cases just happened to appear at the same time, many observers believe that the increased pursuit of such cases reveals a trend that merging parties should take into account when contemplating a transaction that could raise conglomerate effects in the EU. The parties should consider whether customers in the relevant markets might complain during the merger review process. They should also review internal documents to see whether statements were made by the sales and marketing teams about leveraging the merged company's increased strength in one market into other markets. In in-depth antitrust reviews, regulators both in the US and the EU ask companies to produce tremendous amounts of internal documents, which could be relevant to the competition landscape affected by the merger, on very short deadlines. It is important to ensure that the internal documents are not misinterpreted in a way that could jeopardise the antitrust review. Finally, if it is likely that conglomerate concerns are serious, and time is of the essence, the parties could explore whether to raise the issue in pre-notification talks with the authorities, and think of a suitable remedy early in the process in order to be prepared.

## EU overview: Competitive concerns and the remedies

| Merging entities | Concerns | Remedies undertaken |
|---|---|---|
| Bayer/Monsanto | Bayer and Monsanto could decide to bundle or tie sales of pesticide products and seeds, potentially making competitors' access to distributors and farmers more difficult in the advent of digital agriculture, which requires collection of information about farms with the aim of providing tailored advice or aggregate data to farmers. | The bundling concerns were not proven during the in-depth investigation and remedies were offered only in relation to the horizontal concerns of the transaction. |
| Broadcom/Brocade | Potential degradation of interoperability between the merged entity's switch chip and interface cards, which could lead to possible leakage and misuse by the merged entity of confidential information related to competing interface card suppliers. | Broadcom committed to cooperating closely and in a timely manner with competing interface card suppliers to achieve for them the same level of interoperability enjoyed by its own interface cards. |
| Dentsply/Sirona | Dentsply rivals that offered dental consumables would be excluded from accessing Sirona's dental equipment due to denial of commercial and technical information. The fact that Dentsply's offer of consumables was very limited in comparison to its competitors' and that Sirona had entered into long-term licensing agreements with Dentsply's competitors that would prevent it from changing its practices for a significant period, did not change the assessment. | Sirona extended existing licensing agreements with Dentsply competitors for ten years and undertook to continue the supply of all necessary know-how, commercial and technical information to them. |
| Essilor/Luxottica | The merged entity would use Luxottica's powerful brands to force opticians to buy Essilor's lenses by means of bundling or tying, and thus exclude other suppliers. | None. The Commission engaged in extensive market testing, reaching out to 10,000 opticians and receiving feedback from 4,000 third parties, which helped it to understand the market and ultimately clear the transaction with no remedies. |
| Intel/McAfee | Rival security solutions would not have access to the necessary information to use the functionalities of Intel's CPUs in the same way as McAfee. | Intel committed to, among other things, ensuring that vendors of rival security solutions will have access to all necessary information required to use functionalities of Intel's CPUs and chipsets. |
| Microsoft/LinkedIn | Microsoft would pre-install LinkedIn on all Windows PCs, integrate LinkedIn into Office by combining the user databases, and shut out LinkedIn's competitors by not providing them with the technical information that they need to interoperate with Microsoft's products. | Microsoft undertook, inter alia, not to force PC manufacturers and distributors to pre-install LinkedIn on Windows PCs and to allow users to remove it should the manufacturer or distributor decide to pre-install it. |
| Qualcomm/NXP | Interoperability concerns; concerns that Qualcomm would bundle NXP's IP to its patent portfolio, increasing its bargaining power and allowing it to charge significantly higher royalties. | Qualcomm committed to: providing the same level of interoperability between its own products and NXP products with the corresponding products of other companies for an eight-year period; offering certain licences; and not acquiring or enforcing certain patents. |

# Merger remedies: The rise of conditions

Regulators in key global markets are increasingly demanding remedial action to allay competitive concerns

*By Rebecca Farrington, Noah Brumfield, Jérémie Jourdan, Veronica Pinotti, Martino Sforza*

In the European Union, an increasing number of merger clearances are being given on the condition that the parties offer suitable remedies. During Margrethe Vestager's first three years as Commissioner for Competition, a total of 64 conditional clearances have been granted. This constitutes a 42 per cent uplift compared to previous Commissioner Joaquín Almunia's final three years in office.

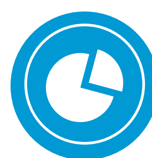
A conditional clearance will most likely require the parties to divest a part of their business, as has been the case for more than 80 per cent of remedy cases over the past three years. (In 2015, 90 per cent of conditional clearances required a divestiture of some kind.) In fact, the European Commission's (EC's) policy explicitly prefers structural remedies—which require merging parties to make divestments that change the market structure—over other types of remedies.

Every remedy has a subtle difference. While the divested business should be viable to allow the purchaser to compete effectively with the merged entity on a lasting basis, the structure of the divestiture may vary to account for competitive concerns. For example, it may affect global R&D facilities to tackle innovation concerns (as in Dow/DuPont), employ a transitional supply agreement to address viability concerns (as in Staples/Office Depot), or licensing arrangements to enable the purchaser to market the divested business under the merged entity's stronger brand (as in Danone/The WhiteWave Foods Company).

There is also now a higher chance that the closing of the deal will be delayed as the EC increasingly requires merging parties to agree to upfront/fix-it-first purchaser clauses.

Usually, merging parties offering remedies can close a transaction once they receive the EC's conditional clearance. A suitable purchaser has to be identified following clearance within a set period. But when the EC has concerns about whether a suitable purchaser can be identified, an upfront buyer or fix-it-first clause can be used. An upfront buyer clause requires the parties to agree not to close the transaction until the EC approves the purchaser and the underlying agreements. A fix-it-first clause goes one step further, and obliges the parties to find a suitable purchaser and enter into a legally binding agreement during the EC's administrative procedure.

In 2015, one in five remedy decisions included an upfront buyer or fix-it-first purchaser clause. By 2016, this number increased to one in three—a trend that continued into 2017, when approximately 33 per cent of decisions imposed a purchaser clause.



**80%**

A conditional clearance requiring the parties to divest a part of their business has been given in more than 80 percent of EC remedy cases over the past three years

**1/3**

In 2017, approximately one in three of all EC remedy decisions imposed an upfront or fix-it-first purchaser clause

**Case of delay**

In practice, these clauses provide leverage to remedy buyers: Merging parties anxious to close may settle for a 'fire sale' of the divested assets. Yet Ball/Rexam is an example of the potential sluggishness of the process. This merger within the global canning sector was conditionally cleared on 15 January 2016 with an upfront buyer clause included in the remedy. Ball had noted pre-clearance that there was 'no assurance that buyers satisfactory to Ball and the regulators' could be found. Indeed, it took three months for Ball to propose a suitable purchaser to the EC. It took another three months for the EC to conclude on the suitability of the purchaser and the underlying agreements, demonstrating the delay the process can cause to closing. The deal finally closed six months after the parties received the EC's conditional clearance decision.

Under Italian merger control rules there is no standstill obligation, therefore, in principle, the parties would be free to close a deal, subject to merger control clearance, after the notification. However, the Italian Competition Authority may order the merging parties to refrain from transacting in the case of pursuing an in-depth investigation, although it has rarely done so in the past (see cases Groupe Canal+/Stream and Autogrill/Ristop, both in 2002). In addition, if the authorisation is ultimately not granted, but the transaction has already been implemented, the authority may order all measures required to restore the pre-merger status, including divestment. For this reason, in most cases the parties complete the transaction conditional upon the authorisation of the Italian Competition Authority. As a consequence, if the transaction is authorised with remedies, whether the deal can close prior to the implementation of the remedies will largely depend on what the parties agreed in the transaction agreement. For instance, in case of structural remedies, the parties must determine whether the acquisition may or may not take place prior to finding a suitable buyer for the divested business, and therefore, who should have responsibility for finding a buyer and run the risk of fines from the Italian Competition Authority for transacting without complying with the remedies, if a suitable buyer is not found. As a reference, the first threshold of the two cumulative thresholds that trigger mandatory notification in Italy has just

been updated from €492 million to €495 million, i.e. (i) aggregate turnover in Italy of all undertakings involved above €495 million; and (ii) individual aggregate turnover of at least two of the parties of the transaction above €30 million.

Although rare, non-structural remedies—such as promises not to act in a certain way in the future—do exist. Over the past three years, 11 out of 64 remedy cases were resolved with a purely behavioural remedy. They are accepted 'only exceptionally in specific circumstances,' such as in 'conglomerate structures'.

For instance, on 25 February 2016, the EC conditionally cleared the conglomerate concerns in Dentsply/Sirona with a behavioural remedy. The EC maintained that the merging parties would have significant market power that could foreclose competing suppliers of dental 'blocks' from a sizeable part of the 'chairside CAD/CAM system' market. To remedy this, the EC required an access remedy from the parties, including the extension of existing licensing agreements with competing block suppliers until 2026. The EC took the unusual step and noted that 'remedies other than divestiture remedies appear best suited to directly address the [conglomerate] concerns raised.'

In November 2017, Qualcomm updated its remedy package to allay the EC's concerns in Qualcomm/NXP Semiconductors. Qualcomm first offered a set of commitments on 5 October 2017. It is understood that the October package offered to carve out all standard essential patents (SEPs) from the transaction, and committed Qualcomm not to assert certain patents owned by NXP (in particular Near Field Communication Technology – NFC). This package was market tested and viewed as inadequate by market participants. The November package added on the behavioural obligation on Qualcomm to ensure the interoperability of NXP's NFC platform with other parties.

Notably, in the most recent merger cases authorised with remedies, the Italian Competition Authority has often imposed a combination of structural and behavioural remedies and in some cases only non-structural remedies. In the RTI/Gruppo Finelco case (2016) the authority requested only behavioural measures, including prohibitng the merged entity from concluding other advertising

**85%**

Of the 33 transactions on which MOFCOM has imposed conditions since the Anti-Monopoly Law (AML) entered into force in 2008, all but five involved foreign-to-foreign transactions

concession contracts, to limit potential vertical and conglomerate effects which could be produced by the merger. In April 2017, in the Gruppo Editoriale l'Espresso/Italiana editrice case the authority also only imposed behavioural measures considered capable of neutralising the horizontal overlaps between the merging parties in the relevant market. In January 2018, in case 2I Rete Gas/Nedgia, the most recent merger case authorised with remedies, the authority imposed structural measures consisting of the divestment of certain local activities as well as behavioural remedies aimed at lowering barriers to entry to the market.

## US approach

In early 2017, the United States Federal Trade Commission (FTC) released a report analysing the effectiveness of past merger remedies (between 2006 and 2012) and outlining best practices going forward. The report confirms the FTC's preference for structural remedies, such as divestitures, over behavioural remedies that often require extensive monitoring to enforce. The Department of Justice (DOJ) has not released a similar official report, but Makan Delrahim, the recently confirmed head of the DOJ Antitrust Division, echoed the FTC's preference for divestiture over behavioural remedies in a recent appearance at New York University.

The FTC report found divestiture of an ongoing business (a set of assets immediately capable of being a stand-alone business) to be more effective than divestiture of selected assets. The distinction focuses on the ease with which a standalone business divestiture may be transitioned to the buyer, compared to assets that take more effort to be incorporated into the buyer's existing framework before successfully competing in the market. For the FTC to accept a divestiture of selected assets, the parties may be expected to show why divestiture of an ongoing business is infeasible and demonstrate how the selected assets can operate as a viable and competitive business.

The FTC also expressed concern over the 'hold-separate' period, during which assets identified to be divested remain in the control of the seller. The FTC stressed the importance of independent managers empowered to make real-time decisions to maintain the assets' competitive value during the interim period before divestiture is complete.

Recent FTC and DOJ enforcement actions have been consistent with this policy directive. For example, the FTC recently required Abbott Laboratories and Alere Inc. to divest two product lines to obtain clearance, and the DOJ ordered CenturyLink and Level 3 Communications to divest certain overlapping aspects of their telecommunications businesses.

## China attracts controversy

In China, the Ministry of Commerce (MOFCOM) has increasingly imposed patent-related remedies on merging parties as a condition to approval. This approach has been criticised for diverging from enforcement approaches taken in other jurisdictions. However, it appears to be an ongoing trend that may create uncertainty, particularly for mergers involving high-tech companies.

To date, a majority of mergers drawing mandatory remedies in China are foreign-to-foreign mergers. Of the 33 transactions on which MOFCOM has imposed conditions since the Anti-Monopoly Law (AML) entered into force in 2008, all but five involved foreign-to-foreign transactions.

Merging parties should be prepared for a prolonged review waiting period, particularly in mergers involving the technology industry. MOFCOM recently imposed a hold-separate period on a high-tech consolidation, a remedy that has not been used in at least four years. This controversial remedy requires the merging parties to ensure various aspects of their operations remain independent for two years. MOFCOM's reviews of proposed high-tech mergers are often influenced by local vendors' objections to sector consolidation.

Since the end of 2014, MOFCOM has penalised non-compliance with imposed remedies, including monetary fines up to ¥500,000 (approximately €64,000). That trend continued into 2017. In addition, MOFCOM maintains jurisdiction to order the dissolution of the merger, disposal of shares or assets, the transfer of the business, or adoption of other measures to restore the market situation. Despite this position, MOFCOM has never yet ordered dissolution of a non-complying merger. To date, all 19 MOFCOM penalties have been monetary fines imposed for failure to file, rather than for post-filing noncompliance.

# Renewed focus on common ownership

The European Commission is paying greater attention to investors who hold stakes in multiple companies in the same industry and considering how this concentration of influence might have an anti-competitive effect

*By Marc Israel*

In recent months, 'common ownership'—whereby investors hold minority stakes in multiple companies active within the same industry—have come under increased scrutiny in the context of merger control. In February of 2018, Margrethe Vestager said that the European Commission is 'carefully' looking into the matter and has begun investigating the extent to which common ownership actually exists.

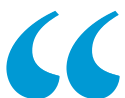
It would not be surprising if the analysis finds the phenomenon quite prevalent, at least in listed companies. That is because many institutional shareholders own stakes in businesses that compete, especially 'tracker funds' which invest in all constituents of any stock market index. While the holdings may not be large in percentage terms, these investors can often be among the businesses' largest shareholders and, in value terms, the stakes are often substantial.

However, one must draw a distinction between the fact that a number of investors may have shareholdings in competing businesses and whether they can influence the decisions of those companies. Various economic studies have investigated the potentially detrimental impact that common ownership can have on competition, and whether the phenomenon disincentivises businesses within the same industry from battling for market share. The value of this kind of research, and the need to expand it, has been recognised by competition authorities. The issue has come under the spotlight again more recently, following the merger between two agrochemicals giants, Dow and DuPont. Speaking last October at UCL's Transformations of Competition Law conference in London, for example, Carles Esteva Mosso, the European Commission's deputy director-general for mergers, signalled that the studies are firmly on the regulator's radar, as Vestager's recent comments have confirmed.

Esteva Mosso noted that the Dow/DuPont case was the first in which common ownership formed a part of the Commission's substantive analysis. He explained that 'the common shareholding in the agrochemical industry' was 'taken as an element of context in the appreciation of any significant impediment to effective competition'.

While the deputy director-general went on to say that no definitive conclusions about the future of the Commission's merger review can yet be drawn, the issue is quite clearly gaining prominence. It should also be noted that, while the analysis given to the issue in Dow/DuPont is unprecedented, the Commission's Horizontal Merger Guidelines mention cross-shareholdings as facilitating possible co-ordinated effects, both by providing a channel for the exchange of information between competitors and in providing 'help in aligning incentives among the coordinating firms'. Though the Guidelines refer to cross-shareholdings between competitors, the underlying issues relating to common ownership—shareholders owning a stake in several competing businesses—are very similar.

So, with this in mind, what are the potential effects on merger review going forward? What would an increased focus on common ownership mean in practice? How might different industries feel the impact?



**The issue has come under the spotlight following the merger between two agrochemical giants, Dow and DuPont**

### Case-by-case approach

First, if common ownership is to form a new focus for the Commission, it is very likely that a case-by-case approach will be adopted. The impact of the issue on competition will vary by industry, and by the specific nature of the activity in which companies are engaging. At its heart, this is because the nature of healthy competition and what drives that varies so widely by sector.

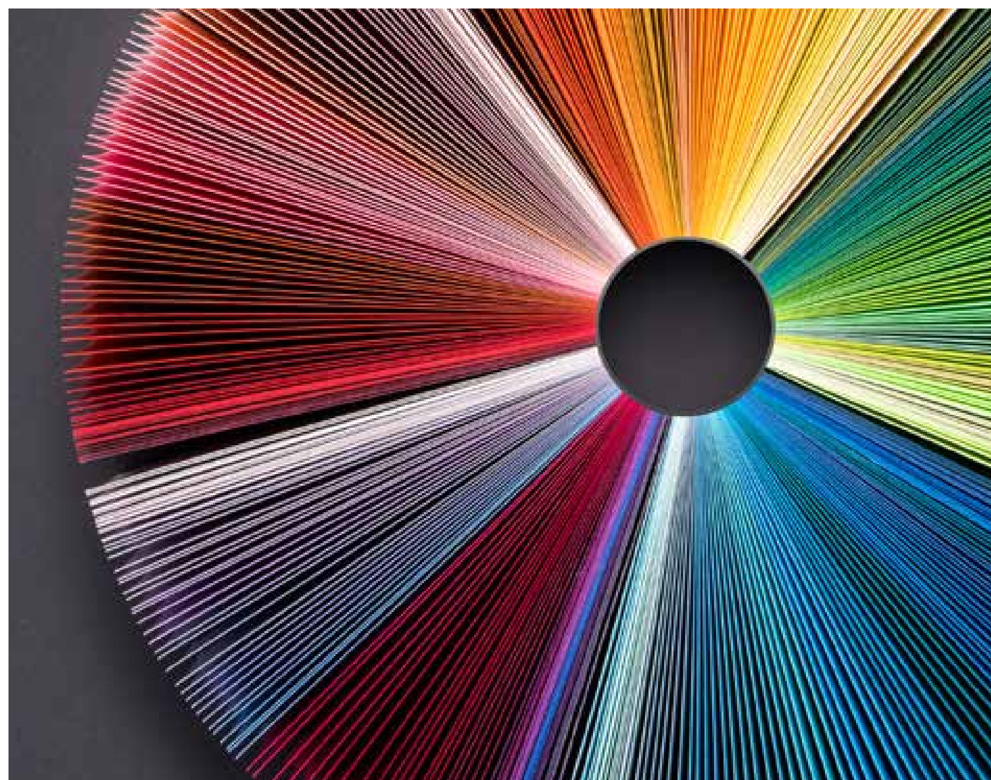
An industry's stage of development is likely to be one of the considerations. The tech sector, for instance, is still relatively young, and innovation is constant. Giants like Apple, as well as a wealth of startups and disruptors, are locked in a fast-paced race to out-innovate one another. Investors often back multiple entities in such a race to hedge their bets, and have at least some stake in whichever company comes out on top with the next best product, platform or system.

Moreover, while the technology sector is consolidating, it is doing so in interesting ways. When large tech firms buy up small ones, they often pit them against one another, treating their

portfolio of companies as bets on the future. In this context, the potentially anti-competitive effects of common ownership may be somewhat mitigated.

In older, more established industries meanwhile, where the scope for innovation is naturally more limited, any impact of common ownership may be more amplified or adverse.

This is not, therefore, a case of one-size-fits-all. How rules are applied and enforced will depend on the specific businesses under scrutiny and the deal under review. Any merger will be analysed in context, with an understanding of how investor activity affects the incentives that companies have to compete.



**Activist shareholders**

In addition, the behaviour of individual shareholders is likely to be a major consideration. In fact, the identities and conduct of those shareholders with common ownership positions are likely to be particularly relevant.

Increased shareholder activism and attempts to influence target companies' management have attracted considerable attention over recent years. Demands for chair resignations, board seats and strategy reviews are increasingly common. In the Dow/DuPont case, Esteva Mosso highlighted the Commission's consideration of what fund managers 'said publicly about how they use their stakes', finding that 'many of them are not simply passively managing the stakes… but interacting with the management' of companies.

This activism complicates the analysis of common ownership positions. Activist investors with stakes in multiple companies within an industry may well seek to exercise their influence in ways that have the potential to dampen competition—whether directly or indirectly. With an interest in the performance of their overall portfolio, they may use their influence to try, for example, to encourage consolidation or a particular direction among the companies in which they hold a stake.

As such, the consideration of common ownership in any particular scenario will involve an examination of how the investors in question exercise their influence, and what that means for competition. In particular, the analysis needs to distinguish between determining the extent to which a shareholder may have a stake in various companies in the same sector and whether it can, or will, seek to influence the decisions of those companies.

**Mission creep**

It is interesting to look at the new focus on common ownership within a broader context. Some view the developments as part of a wider drive by the European Commission to expand its remit and the boundaries of merger control more generally. Is this a case of mission creep?

Proposals to expand both the range of deals and specific issues covered in the Commission's merger review analysis have been under consideration for some time. For example, the Commission does not currently possess the authority to assess the acquisition of minority stakes under its merger control rules and has considered proposals to allow it to do so, as authorities in the UK, Germany and Austria can. Similarly, the Commission has also recently proposed a framework for screening foreign direct investment (FDI), raising potential national security or public order concerns. Initiatives like FDI screening or looking at common ownership may indicate a general attempt by the European Commission to cast its net wider and broaden its reach.

Companies and advisers should follow these developments closely, to ensure they are prepared for any change in direction or expansion of Commission activity. With Brexit approaching, this is a particularly important time for businesses with UK operations—the UK's exit from the EU presents an opportunity for competition authorities at both a national and European level to review their position and set the tone for the coming months on some of these issues.

**Looking ahead**

It is still early days. Esteva Mosso himself has said companies should not read too much into the approach taken in the Dow/DuPont case. It may well be that this is nothing more than a storm in a teacup—time will tell.

It is important, however, that companies and investors understand this issue. It is likely the Commission and other competition authorities will monitor any new research or findings on the subject of common ownership closely, especially if activist investors continue to seek to drive the policy of the companies in which they may only own a very small stake. It seems unlikely that Dow/DuPont will be a one-off case, and we may well see common ownership becoming a feature of merger analysis in the future, in cases where a number of competitors in a particular industry are listed companies, and may therefore have a number of common shareholders.

# Avoiding the merger control blues

Effective handling of antitrust issues can help businesses bolster their negotiating position—whichever side of the deal they're on

*By Patrick Sarch, Sophie Sahlin*

Delays or derailment of a deal by merger control considerations can significantly impact the commercial returns for both parties. But there are a number of steps that businesses can take to mitigate the risk.

**Avoid unnecessary 'triggering events'**

In the majority of jurisdictions, a filing is triggered only if there is a 'change in control', meaning that a party acquires de jure or de facto joint or sole control over the target. Typically, the acquirer obtains sole control if it alone can decide on strategic matters, such as the budget, business plan, major investments and appointment/removal of senior management. The acquirer would obtain joint control if it can block such decisions ('veto rights').

There would be no change in control if the acquirer obtains a non-controlling minority stake in the target company or if the transaction results in 'shifting alliances', where each strategic decision is approved by a different combination of shareholders.

Some jurisdictions, however, have chosen to create additional 'triggering events' that may cover situations in which an acquirer is not seeking control. For example, the acquisition of a certain percentage of shares or votes in a company constitutes a notifiable transaction in a number of jurisdictions, such as Austria, Germany and Brazil.

In a minority of jurisdictions, a transaction constitutes a notifiable transaction where the acquirer obtains some form of 'material influence', but less than control. In Germany, for instance, the acquisition of the 'ability to exercise competitively significant influence' constitutes a notifiable transaction. This provision is triggered when the acquisition of less than a 25 per cent stake is accompanied by so-called 'plus factors', such as information rights, the right to appoint board members or certain blocking rights. Although not very commonly used, this provision is relevant where the investor is a strategic acquirer with stakes in competing businesses.

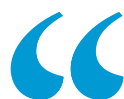
Delays caused by notifiable transactions can significantly impact the commercial returns for both parties. Therefore, it may be more commercially attractive to structure the deal to ensure that there is no triggering event. However, it's important to ensure that the structure and deal documentation reflects the parties' true intentions, as competition authorities will assess the economic reality of the transaction and consider whether a situation may give rise to de facto control.

**Make use of a put and call option agreement**

Entering into a put and call option agreement allows the parties to postpone a filing obligation up to the moment in time when the option is exercised, and where a filing obligation may no longer interfere with deal imperatives or competitive conditions may have changed.

There are two scenarios in which such a move could delay timings of aspects of the transaction that may lead to trigger events: where an acquirer is attempting to purchase multiple businesses; and where an acquirer is looking at a large business that can be carved up to be acquired in stages. In the first of these scenarios, acquirers may wish to combine two similar or complementary targets to create synergies, which can give rise to antitrust scrutiny.

Even if the transactions are undertaken separately (i.e., no mutual conditionality) such that separate filings are triggered, both sets of competition authorities (which may or may not be the same) will review the combination if the transactions run in parallel (i.e., simultaneous closing). Even if they are sequential but overlap to some extent, such that the competition authorities reviewing the second of the two transactions would review the combination, the combination would in practice impact the review by the first set of authorities (in particular if the same authorities review both transactions). This could delay closing of both deals, which can put an acquirer at a disadvantage notably in a competitive bidding context. The acquirer would therefore have to balance two potentially conflicting priorities: ensuring that it signs both deals to realise the envisaged synergies, while not jeopardising its chances of signing



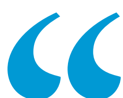
**Some jurisdictions have created triggering events that may cover situations in which an acquirer is not seeking control**

each one of them because of the implications the combination may have on the process.

One way to manage this balancing act is to proceed with the more pressing deal first and agree on a put and call option on the second deal. Provided that the second seller is willing to wait, the potentially problematic combination is not reviewed until the acquirer exercises the option, which allows the acquirer to put forward a competitive offer for the first deal while securing both deals.

Where the acquirer is looking at one target which alone gives rise to competition issues, it may be possible to acquire part of the business (for example, one manufacturing plant) or a minority stake initially, alongside a put and call option for the remainder of the business. At the point that the acquirer decides to exercise the option, competitive conditions may have changed or the parties could have used the longer lead time to develop remedies to tackle the authorities' scrutiny.

When exercising staggered acquisitions of several parts of a business involving the same acquirer and seller in the EU, even for acquisitions which are not mutually conditional, extra caution needs to be taken. Even if each individual acquisition would not trigger any filing obligations because the revenue of each part does not hit the filing thresholds, all the staggered transactions involving the same acquirer and seller over a period of two years' time would become notifiable with the most recent acquisition, if one or several of the transactions taken alone or together triggers the revenue filing thresholds.



**The parties can carve out assets likely to be causes of concern to the authorities before launching the transaction**

**Offer an up-front carve-out or remedies**

If a merger filing is required and it is expected to give rise to in-depth scrutiny, the acquirer can ensure that competition concerns are addressed up-front to avoid slowing down the overall process.

The parties can carve out assets likely to be causes of concern to the authorities before launching the transaction. However, it must be made clear to the authorities reviewing the transaction that the carved out assets will not fall within the scope of the main transaction nor their review. The authorities will also want to satisfy themselves that the problematic assets have indeed been carved out before the main transaction closes.

An alternative to an up-front carve out is up-front remedies, where the parties offer a comprehensive and clear-cut remedy package in Phase 1 to avoid going through the lengthy and in-depth review of a Phase 2 investigation.

# Private equity and merger control: Increasing buyer scrutiny

The evolution in private equity means that forward-thinking firms are adding early-stage review to their merger strategy

*By Pontus Lindfelt, Matteo Giangaspero*

The merger control assessment for transactions involving private equity firms has become increasingly complex as, over the years, they have grown to become industry giants with a well-established industry presence. Today, they typically control a large number of portfolio companies and tend to focus on investment in clusters or specific sectors. Moreover, private equity transactions often have a clear industrial rationale driven by pre-existing portfolio companies and do not constitute a mere financial investment.

In the majority of cases, therefore, the establishment of filing requirements requires a thorough assessment of the control structure of the fund involved in the transaction in order to identify the relevant turnover for the merger filing analysis. When it comes to substantive assessment, complexity derives from the need to cover potential horizontal overlap and any vertical relationship between the private equity portfolio companies and the targets.

An upfront merger filing analysis including the substantive review has become an essential part of the overall deal, and will include—in certain cases—establishing whether (and to what extent) remedies will be needed to obtain timely clearance.

**Transaction triggers**

Transactions involving private equity firms are often subject to merger control requirements because their turnover exceeds the relevant thresholds and normally result in a change of control over a target. In most cases, to establish whether a competition authority has jurisdiction over a transaction, the relevant turnover to be taken into account will be the financial income of the private equity firm and the revenue generated by all its controlled portfolio companies, which are deemed to be part of the same 'group.'

The notion of control encompasses rights, contracts or any other means which, either separately or in combination, confer decisive influence on an undertaking.

The private equity firm will typically acquire sole control over a target by acquiring: (a) the entire capital; (b) a majority interest; or (c) a minority shareholding that confers veto rights over the target's strategic decisions. Veto rights resulting in (negative) joint control relate to decisions on matters such as the target's budget, business plan, major investments or appointment of senior management.

In other cases, the private equity firm will acquire joint control over the target, either together with another private equity firm or institutional investor or together with pre-existing shareholders or the founders of the target. The acquisition of joint control increases the likelihood of merger filing requirements. The assessment of whether the private equity firm will be acquiring control requires a case-by-case analysis, which would be conducted both on a de jure basis and a de facto basis, in particular when the founders are still involved—as shareholders and/or as managers—in the business of the target. Even the acquisition of a minority stake above a certain percentage without any controlling rights may trigger filings in EU Member States (for example Germany and Austria) and in extra-EU jurisdictions.

**10%**

The EU Commission can impose fines of up to 10 per cent of worldwide group turnover for intentional or negligent breaches of a standstill obligation

The EU Commission's Jurisdictional Notice 139/2004 describes control as the 'power to determine strategic commercial decisions' of another undertaking (so-called 'positive control') or the power to veto such decisions ('negative control'). In this regard, the Jurisdictional Notice provides guidance on transactions involving investment funds.

The Jurisdictional Notice notes that '[i]nvestment funds are often set up in the legal form of limited partnerships, in which the investors participate as limited partners and normally do not exercise control, either individually or collectively.' As such, investment funds tend to acquire shares and voting rights that confer control over portfolio companies in their capacity as mere investment vehicles. Control is then ordinarily exercised by the investment company that has set up the fund, not the fund itself, through the investment group's organisational structure—for example by controlling the general partner of the funds and/or by contractual agreements, such as advisory agreements. In that way, the investment company generally acquires at least indirect control over the portfolio companies held by the investment funds.

**Different fund structures**

Although the Jurisdictional Notice provides general guidance, the corporate

structures that involve investment funds must be assessed on a case-by-case basis. Often, private equity firms are organised through different funds, and each of these funds controls a number of portfolio companies. In some cases, it could be argued that the fund involved in the transaction is not part of the same 'group' as the other funds, and that therefore these should not be taken into account for turnover purposes or in the substantive assessment. To support such a position, it may be helpful to show that funds within the same private equity firm are managed by different general partners. However, this may not be sufficient to persuade the EU Commission (and other competition authorities) if, for instance, the same managers are board members of different general partners established by the private equity firm or if the general partners are supported (or supervised), for instance, by the same investment committee or advisory committee. In addition, by structuring each fund independently and by taking this position before competition authorities, private equity firms would have to carefully implement effective safeguards to avoid any coordination and exchange of competitively sensitive information between the funds and portfolio companies controlled by the different funds. This may increase the risk of Article 101 TFEU infringements.

In a few cases, a limited partner may hold more than half of the limited partnership of the fund. This may be the case for a large institutional investor. Although it is unlikely that the limited partner exercises any controlling rights over the investment fund, its turnover would still be relevant to establish merger filing requirements.

**State influence**

There is also an increased tendency in the public sector—for instance in China and in the Gulf area—to establish investment funds acquiring controlling stakes in European companies. Although these investment funds may be set up in the legal form of limited partnerships, public authorities may still exercise (indirect) control over them. Any link between the management of the fund and public authorities may raise questions about the possibility for the state to exercise decisive influence over it. In addition, a public entity (alone or together with other public entities) acting as a limited partner—especially in cases with a large shareholding in the limited partnership—may raise questions as to the independent exercise of investment and other strategic decisions by the fund. In short, a case-by-case analysis is needed to establish whether the investment fund shall be viewed as a state-owned entity, to which specific merger control rules may apply.

As these examples show, considering all funds (and their respective portfolio companies) as part of a single economic entity for merger control purposes may not necessarily reflect the actual structure of a private equity firm. That said, there are a few jurisdictions (including the US and Canada) that diverge from this approach: In these jurisdictions merger control rules are applied to the fund(s) involved in the transaction being assessed, rather than to the private equity 'group'.

**EU developments**

In October of 2016, the EU Commission launched a public stakeholders' consultation on evaluation of procedural and jurisdictional aspects of EU merger control. Two aspects of this consultation are of particular interest for private equity transactions.

First, the EU Commission is contemplating the introduction of a deal size threshold, complementary to the current turnover thresholds. A likely consequence of the additional threshold is that more transactions would be caught at the EU level, resulting in additional burdens for private equity firms, especially for those investing in new technology businesses.

The EU Commission is also considering extending the scope of application of the EU merger control simplified procedure. Broadening its application to transactions involving a vertical relationship and to acquisitions of joint control over a target with no activities within the European Economic Area territory would contribute to a reduction of the burden on private equity firms involved in transactions that do not present substantive issues.

As in most jurisdictions, the parties acquiring control in a transaction that meets the EU jurisdictional thresholds are required to notify the EU Commission and are subject to a standstill obligation barring them from implementing the transaction before clearance. The EU Commission can

**Competition authorities usually welcome informal remedies discussions at the early stage of the notification process, and even during the pre-notification phase**

impose fines of up to 10 per cent of worldwide group turnover for intentional or negligent breaches of such an obligation. With the EU Commission (and other competition authorities in Member States and worldwide) cracking down on breaches of gun-jumping rules and of the standstill obligation (for example in Case M.7993, Altice/PT Portugal, Altice was recently fined €125 million), private equity firms must carefully assess their filing obligations and ensure they obtain clearances prior to completing their transactions or exercise any control over the target companies.

Moreover, the EU Commission can impose fines of up to 1 per cent of worldwide group turnover for intentionally or negligently supplying incorrect or misleading information in the context of merger control filings, regardless of whether the information has any impact on the EU Commission's decision. The EU Commission is actively enforcing its powers in this context (see the fining decision in Case M.8228, Facebook/WhatsApp and the ongoing investigation in Case M.8436, General Electric/LM Wind), and it recently stressed the importance of complying with the obligation to provide correct information, in order for it to be able to make decisions 'in full knowledge of accurate facts'. Therefore, it is crucial for private equity firms, as notifying parties, to ensure that information provided by all the parties involved in the transaction, including the portfolio companies and the target, is accurate and complete.

**Evolution**

So, while the large majority of private equity transactions still do not present substantive issues, having no (or limited) overlap with the targets' activities, private equity firms' increasingly large portfolios may trigger competition issues. In this respect, the rules of the game have changed for private equity firms involved in controlled auctions. Where in the past the absence of any competition issues often gave an advantage to private equity buyers, today overlaps with other portfolio companies are more frequent and industrial bidders may have an advantage.

This evolution requires private equity firms to conduct an in-depth assessment of the potential horizontal overlaps and vertical links between the target and the portfolio companies. Where the private equity firm controls a large number of portfolio companies active in the sector of the transaction, the data-gathering process may prove very burdensome. Moreover, in cases in which a private equity firm is contemplating joint control together with a co-investor (for instance, another private equity firm), the assessment of horizontal overlaps and vertical links must be extended to the co-investor's activities and its portfolio companies.

Therefore, it is recommended that this analysis be conducted up-front, allowing—in the case of competition concerns—early-stage remedies to be proposed, especially where a deal is time-sensitive. Competition authorities usually welcome informal remedies discussions at the early stage of the notification process, and even during the pre-notification phase, where applicable. Such discussions increase the chances of obtaining a conditional clearance (subject to remedies) in Phase I and mitigate the risk of competition authorities opening lengthy in-depth (Phase II) investigations. Negotiating a remedy package in Phase II may also increase the risk for private equity firms of having to divest certain assets, or an entire business, under time pressure and with limited bargaining power.

Also, transactions with a clear rationale to consolidate the business of one of the portfolio companies could, in theory, trigger a 'conflicting interest' between the private equity firm and the portfolio company, with the private equity firm being typically more risk-averse on competition issues than its portfolio company.

Ultimately, private equity firms now need to take a more strategic approach to merger control issues. They must be pro-active in conducting merger control analysis before initiating a transaction. A good understanding of filing requirements and substantive issues (if any) is crucial in coming up with a plan to address any issues up-front, to avoid lengthy Phase II investigations and allow transactions to close without undue delay.

# Raising the global bar for security clearance of cross-border transactions

A clampdown by governments across the world on potential security threats has increased the scrutiny of participants seeking clearance for cross-border mergers and acquisitions

*By Tobias Heinrich (Germany/EU), Marc Israel (UK), Farhad Jalinous (USA), Igor Ostapets (Russia), Veronica Pinotti (Italy), John Tivey (Australia), Jun Usami (Japan), Alex Zhang (China), Orion Berg (France), Ksenia Tyunik (Russia)*

With governments around the world placing foreign direct investment under ever greater scrutiny, an increasing proportion of big cross-border mergers and acquisitions are being subject to national security review procedures. Keeping abreast of new laws and engaging early with national bodies has never been more important when navigating this new landscape.

## Australia

**Infrastructure security spotlighted**

The Foreign Investment Review Board has the power to intervene on any transactions that lead to the acquisition of a 'substantial interest' in an Australian company, land, land-rich entities, agricultural land and agribusiness, or acquisitions by foreign governmental investors. The Treasurer may prohibit or order broad divestments when a transaction appears contrary to the national interest based on its impact on national security, competition, government laws and policies, the economy and community or the investor's character. In January 2017, the Australian government launched the Critical Infrastructure Centre to independently advise the Treasurer on national security risks in respect of access and control of the country's critical assets, such as ports and storage, and energy supply. In March 2018, the Security of Critical Infrastructure Act was passed to give the Minister for Home Affairs a broad power to take action to protect against threats of espionage and foreign interference to critical infrastructure. The legislation established a register of Australia's high-risk critical infrastructure, including information on asset ownership, access and control.

## Canada

**Increased transparency is encouraged**

The Canadian government has the power to review transactions that exceed a specific threshold or transactions (including minority investments) where there are 'reasonable grounds to believe that an investment by a non-Canadian could be injurious to national security'. Although there is no definition for the latter, authorities' examination of the potential effects on national security include the areas of defence, technology, and critical infrastructure and supply. Parties in a transaction raising national security concerns are encouraged to seek clearance at least 45 days before closing. Authorities can block the investment, ask for undertakings and/or provide terms or conditions. Recent trends show an encouragement of foreign investment, prompting the government to issue guidelines that increase transparency.

## China

**Cybersecurity law adds requirements**

In 2011, China's Ministry of Commerce (MOFCOM), the regulatory body that has oversight for reviewing acquisitions, introduced a set of temporary provisions aimed at assessing the overall impact of foreign investments on China's national security, defence, economy and public interest. In 2015, China promulgated its first National Security Law, which provides more detailed rules under which MOFCOM will review, approve or terminate any transaction and to impose sanctions or divestments on acquiring companies. In addition, China's 2017 Cybersecurity Law provides for additional requirements to be placed on companies engaging in critical informational infrastructure or network and data operations.

## EU

**Juncker outlines new measures**

In September 2017, European Commission President Jean-Claude Juncker outlined legislative measures on the screening by EU Member States of foreign takeovers and investments following a significant increase of foreign direct investment into European technology assets, particularly from companies in China with links to the Chinese government. The proposed EU Regulation, which can still be amended by the EU legislature (Parliament and Council), and is currently expected to be passed by the end of Q1 2019, stops short of forcing Member States to establish or maintain investment review mechanisms. However, if they do so, frameworks should be in line with EU law. According to the non-exhaustive list of pertinent considerations, critical infrastructure

**25%**

ownership of an entity performing activities deemed of 'strategic importance' to Russian national defence and security will trigger the need for approval for potential foreign acquirers

and technology, security of supply of critical inputs, and access to or control of sensitive information are included. The new screening system aims to improve cooperation between Member States in vetting transactions affecting security and public order, although the Commission's views are not binding and an ultimate decision rests with the Member States.

**New 'Pacte' law will extend the foreign investments control mechanism**

All foreign investors are required to file a request for prior authorisation over defence, security-related activities and dual-use technology, or activities such as gambling by non-EU investors, so that potential harm to public order, safety or national security can be assessed. The Ministry of Economy may authorise the transaction unconditionally, subject it to mitigating conditions or prohibit it. Prior clearance of the transaction should constitute a condition, whereas buyers should consider including break-up fees or opt-out clauses if conditions imposed are too burdensome. The French Government is contemplating amending the current legal framework in the Loi PACTE (Plan d'Action pour la Croissance et la Transformation des Entreprises – action plan for business growth and transformation) and is debating the law in Parliament. Notably, it will set up a list of sensitive French groups that deserve particular attention. This list will be monitored monthly by a Council of defence and national security comprised of relevant ministers. The French Government will extend the list of sensitive sectors subject to review notably to digital data storage, artificial intelligence, nanotechnologies, financial infrastructures and robotics. Sanctions for infringement to mitigations requirements will also be refined (for example, suspending the voting rights of the foreign investor and introducing fines based on the turnover realised by the target company). It is also expected to help introduce state 'golden shares' in certain strategic assets and use Bpifrance state funds to encourage engagement in the event of hostile takeovers of French strategic businesses by foreign investors.

**Amendments introduce new criteria**

German law provides for a cross-sectoral review of transactions by non-EU/EFTA-based investors in all industries that are likely to pose a serious threat to public

order or security. Recent amendments introduced a non-exhaustive list of criteria to determine the threat. The Ministry of Economic Affairs and Energy can also review sector-specific transactions in sensitive industries, such as arms, military equipment, encryption and other key defence technologies. Foreign investors are generally advised to apply for a clearance certificate in early stages of a transaction. Furthermore, there are proposals to reduce the entry level for foreign investment reviews from a 25 per cent threshold down to 10 per cent in equity and/or voting rights.

## Italy

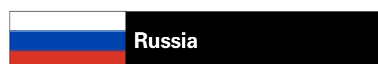
**Shares acquisitions may be subject to scrutiny**

In Italy, the acquisition of shareholdings of companies engaged in activities deemed to be of strategic importance may be subject to certain limitations by the Italian Government (so-called Golden Powers). In particular, in case of purchase of shareholdings in strategic businesses operating in the defence and national security sectors, the Italian Government may impose specific conditions in relation to the security of supply, the security of information, technological transfers, and the control of exports. On 16 October 2017, in the context of the Vivendi-TIM transaction, the Italian Government exercised this power for the first time, imposing restrictions on certain strategic assets including a network unit and a software division. Both companies have challenged the decision before the President of the Italian Republic and the case is currently pending.

## Japan

**2017 sees enhanced enforcement**

Japan's Foreign Exchange and Foreign Trade Act authorises the competent ministry to review the acquisition by a foreign investor of shares, loans and bonds of a Japanese company (known as inward direct investment), as well as the acquisition of shares of a non-listed company from other foreign investors (designated acquisition), and to change the content or discontinue the transaction. Designated acquisitions are subject to advance notice where they are relevant to Japan's national security. Advance notice is also required for inward direct investments if they affect national security, public order or safety, the Japanese economy, or involve investors from certain countries. In 2017, amendments were introduced to widen the scope of review and enhance enforcement mechanisms.



## Russia

**Review extended to reach off-shore companies and potentially any transactions posing a threat to the national defence and state security**

The Government Commission on Control over Foreign Investments in the Russian Federation is responsible for reviews. It oversees transactions that result in acquisition of control over Russian entities engaged in activities of strategic importance. Currently, the law lists 46 activities that include both those directly related to the state defence and security, and certain other indirectly related activities, such as TV and radio broadcasting over certain territory, extraction of water resources and publishing activities. The criteria for determining control are wide and vary according to the target in question. Foreign investors must also obtain the Government Commission's consent for certain transactions involving acquisition of a strategic entity's property. Foreign public investors are not permitted to obtain control over 'strategic' entities or acquire more than 25 per cent of their property, and must obtain Commission consent for acquisitions of the reduced stakes in strategic entities. The special, stricter regime established for such investors has recently been extended to 'off-shore companies' in jurisdictions such as the United Arab Emirates, Jersey, British Virgin Islands and Bermuda.

The statutory period for reviewing the application is three months from the date of its acceptance for review. The Commission can extend the review period for an additional three months. In practice, the review depends on the availability of the Commission's members and may take longer. The Commission may approve a transaction with or without certain obligations of the foreign investor or reject it. Amendments to the law introduced in 2017 gave the Commission Chairman the right to decide that approval is required with respect to any transaction by any foreign investor with regard to any Russian company (not necessarily strategic) if this is needed to ensure national defence and state security. As such, the definition of 'foreign investor' was extended to include Russian nationals holding other citizenships and Russian companies under foreign control.

**45 days**

The minimum period required for parties in a Canadian transaction raising national security concerns to seek clearance before closing

## UK

**Proposals aim to strengthen powers**

While acquisitions in sensitive industries do not require prior approval, the Secretary of State for Business, Energy and Industrial Strategy (SoS) may intervene under the Enterprise Act 2002, based on public interest considerations related to national security, media plurality, quality and standards, and stability of the financial system. If the SoS intervenes, the Competition & Market Authority (and Ofcom in media cases) will investigate and report to the SoS who will then decide whether the transaction should be subject to a Phase II review or accept undertakings. The Government recently reduced the thresholds for intervention in cases involving military or dual-use (i.e., military and civilian) goods, computing hardware and quantum technology. In addition, recent proposals consider introducing a mandatory notification regime for the civil nuclear, defence, energy, telecommunications and transport sectors.

## USA

**New legislation would extend investment oversight**

The Committee on Foreign Investment in the United States (CFIUS) has the authority to review any transaction that results in foreign control of a US business. Under the Trump administration, there has been rising sensitivity towards in-bound investment and acquisitions by Chinese companies, as well as investment from traditional allies in certain sectors. Politicians have proposed strengthening the CFIUS process against emerging threats in sensitive technologies and in November 2017, US Senator John Cornyn and Representative Robert Pittenger introduced the Foreign Investment Risk Review Modernization Act of 2017 (FIRRMA), which intends to expand the scope of the CFIUS review process. As currently proposed, the legislation would extend the CFIUS review time frames, increase the scope of transactions subject to CFIUS's jurisdiction, make certain notifications mandatory, and establish a process for expedited review of certain transactions.

# Taking back control: Brexit's impact on merger rules

Whether it is 'hard' or 'soft', a UK exit from the EU will mean a very different dynamic in terms of merger control

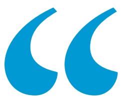
*By Marc Israel*

There has been much debate about whether there will be a 'hard' Brexit or 'soft' Brexit and the impact that each of these outcomes might have on the UK's future relationship with the rest of the European Union (EU), especially in areas such as financial services and as regards the extent to which 'passporting' rights will continue.

However, when it comes to merger control, the type of Brexit that ultimately occurs is irrelevant. Once the UK leaves the EU, mergers and acquisitions that meet relevant thresholds will be subject to review by both the European Commission (EC) and the UK's antitrust body, the Competition and Markets Authority (CMA). Post-Brexit, larger deals that previously met the EU's turnover thresholds and were reviewed under the 'one-stop-shop' principle will be subject to review by both the EC and the CMA. While the UK's merger control system will remain voluntary, many cases reviewed by the EC will no doubt also be notified in the UK (or called in for review by the CMA if parties decide, often for very good reasons, not to notify in the UK).

**Increase expected**

The CMA has reviewed an average of 70 merger and acquisition deals per annum over the last three years and Andrea Coscelli, the CMA's chief executive, says he expects that post-Brexit that number could jump by between 30 and 50 per year.

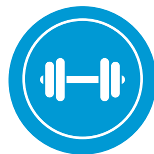


**Leaving the EU will give the UK power to intervene in cases on non-competition grounds in respect of mergers that would otherwise have been subject to review only by the EC**

Further, Coscelli expects that around half a dozen of these will likely be subject to an in-depth Phase II investigation (i.e., akin to a second request in the US). With its workload set to rise by around 50 per cent, the CMA is already planning how to cope with the additional burden on its resources, including seeking additional funding from the UK Government.

In terms of substance, the way in which mergers are reviewed will not be affected by Brexit, and economic-based assessment will continue. Procedurally, the CMA can be expected to continue to work closely with the EC and the national competition authorities (NCAs) of the remaining Member States. However, as the CMA will no longer be a member of the European Competition Network—a forum in which the EC and Member State NCAs cooperate—Brexit may hamper efficient dialogue between the CMA and EC/NCAs, especially when each or several of these bodies are assessing the same merger. It may become more difficult to exchange information about a case without seeking and obtaining specific waivers from the merging parties involved.

Inevitably, some cases will raise competition concerns in the UK and in other jurisdictions and so discussion about the competitive effects of a case, and coordination of effective remedies, will be important.



**50%**

With its workload set to rise by around 50 per cent, the UK's Competition and Markets Authority is already planning how to cope with the additional burden on its resources

**Power gain**

From a policy perspective, leaving the EU will give the UK power to intervene in cases on non-competition grounds in respect of mergers that would otherwise have been subject to review only by the EC. That is because the EC's rules limit the ability for Member States to intervene in mergers subject to the EC's exclusive jurisdiction to specified grounds (public security, media plurality and prudential rules).

Post-Brexit, these limitations will not apply to mergers that fall within the CMA's jurisdiction. With the UK currently consulting on amendments to its merger rules to cover a wider range of foreign direct investment issues, certain mergers reviewable by the CMA may be subject to both a competition test and a wider public interest-style test. For example, MPs have urged the government to intervene in Melrose's bid for GKN.

Whether there is a 'hard' or 'soft' Brexit, companies and their advisers — as well as the CMA—will have to get used to a different dynamic in terms of merger control once the UK leaves the EU. While the voluntary system of UK merger control is expected to remain, should parties decide to notify a deal in the UK, this will inevitably add to the time and cost of securing clearance.

Post-Brexit, merger control will stay the same only if the UK becomes a member of the European Economic Area (following in the footsteps of Iceland, Lichtenstein and Norway), because the EC's exclusive jurisdiction to review mergers that meet its thresholds extends to cover EEA Member States.

# Navigating cultures at Toyota Industries

Toyota Industries Corporation, a company whose roots go back to the early 1920s when Sakichi Toyoda founded his company to produce the Type G automated loom he invented and from which Toyota Motor Corporation was spun off in 1937, is today a global business focusing on material handling equipment, car components and textile machinery. **Taeko Kojima**, general manager of Toyota Industries' legal department, and **Yusaku Inoue** from the department's international affairs group, discuss the Japanese approach to mergers

**What would you consider to be the hallmarks of the Japanese business culture's approach to mergers?**
Japanese companies are very careful in identifying acquisition targets that fit with their corporate strategy and vision. They might be filling a gap in the company's offerings, or supplementing a product range. At management level, a company will examine trends in its market sector and consider whether the target will integrate smoothly into the company. At the legal level, we expect our lawyers to ensure we will be able to close the deal by setting up the proper legal structure and documentation. Japanese companies value due diligence and like to take the time to do it properly. They like to look at all the angles, consider things deeply, and try to rule out surprises.

**Are there advantages or disadvantages to this approach?**
The advantage of this cautious due diligence process is that, having examined all the documentation carefully before closing, potential difficulties are identified in advance and can be dealt with. The gap between expectation and reality is therefore reduced. Having multiple people involved in the decision-making process means that the M&A team knows, once the decision is reached, that it may proceed with a clear mandate.

Yet, this process can hit a wall when the company is bidding publicly for a target against another company: In the European Union and the United States, the corporate culture favours moving very quickly; as globalisation continues apace, Japanese companies will, on occasion, have to accept a shorter due diligence process, depending on the level of interest in the target company.

**In your experience, does the merger control process ever produce surprises?**
Merger control seems to have a small degree of unpredictability. In part, that is because so many countries have merger control regimes, which are often applied and interpreted in slightly different ways. We in the legal department, together with our advisers, spend a lot of time preparing and planning for a smooth review process, taking account of local differences.

Nonetheless, unexpected issues can always arise during the review process. For example, we once were unexpectedly confronted with a foreign investment issue which risked delaying the closing by a few months; ultimately it was a non-issue, but it certainly kept the tension up for a few days.

**What was your biggest take-away from that situation?**
Merger control can often be a political process as much as a business one. It is important to engage with the authorities at every step of a deal, explaining how our industry works and what our goals for the transaction are. Essentially, we have to let them get to know us well.

# Japan: Big Data and the big reveal

In the past 18 months, Japan's regulator has tackled Big Data, introduced greater disclosure and conducted a high-profile, parallel merger review

*By Toshio Dokei, Hideo Nakajima, Seiji Niwa, Takako Onoki*

The pervasive influence of data has prompted the regulator in Japan to rethink its approach to merger control regimes. In June 2017, the Japan Fair Trade Commission (JFTC) and the Competition Policy Research Center (CPRC) jointly published their *Report of Study Group on Data and Competition Policy*. The study group began in January that year and the report discussed how Japan's Anti-Monopoly Act (AMA) can address issues created by today's data-driven society.

**Defining markets**

The JFTC is the sole regulatory authority that enforces merger control under the AMA, and when analysing a business combination, it starts by defining what constitutes a market in terms of size and geographic scope.

The JFTC looks at this from the perspective of a consumer's ability to purchase a substitute product or service, and may also analyse the issues from the vantage point of supplier substitutability.

Traditionally, substitutability is determined using the SSNIP test (small but significant and non-transitory increase in price). But the proliferation of data requires a different approach. The report highlights that a digital platform comprises several layers of markets with different types of consumers or users (also referred to as a 'multi-level market'), where 'free' services might be provided in one market (for example, the social media service market) but compensation is paid in another (for instance, the online advertisement market). The report argues that the SSNIP test does not necessarily apply to this type of 'free' market, and suggests considering the substitutability of consumers and/or suppliers using another method, such as the SSNDQ (small but significant and non-transitory decrease in quality) test, which focuses on functionality and quality rather than price.

**Pre-notification amendments**

When determining whether or not a specific business combination should be reported, the JFTC currently looks only at the parties' Japanese turnover for the previous business year. If their turnover does not meet the thresholds, JFTC pre-notification is not required, even if their turnover may dramatically increase after the business combination is consummated (that is, if the following year's turnovers greatly exceed the thresholds for pre-notification), and even if such a business combination then exerts a substantial influence on the relevant market(s).

The report recognises that it may take some time for data resources to be converted into increased turnover from innovation and/or sales of new products or services. In addition, the aggregated accumulated data may result in the parties being able to obtain or strengthen market power. The report therefore suggests considering a revision of the current pre-notification requirements to allow the JFTC to review certain important transactions that may be missed under the current system. It refers to a 31 March 2017 amendment to the German business combination regulations, which adds the value of an acquired company as a factor in determining whether or not pre-notification will be required. Under such a system, pre-notification could be required even in a situation where the turnover of the interested parties does not meet the thresholds.

**We are hoping to get more information from the JFTC in the future, for example regarding analyses of market definition in real-life cases**

**45**
In 2017, the JFTC reviewed approximately 45 relevant markets when analysing two high-profile mergers

**Information disclosure**

In November 2017, the JFTC introduced quarterly disclosure for proposed business combinations including the following information: filing date; the names of the parties involved; major business category; type of business combination (for example, merger or share acquisition); clearance date; and whether the waiting period was shortened.

The cases cover both Phase I and Phase II combination reviews, subject to the exclusion of some confidential

cases. The new level and frequency of disclosure by the JFTC is a welcome and positive development. We are hoping to get more information from the JFTC about this issue in the future, for example regarding analyses of market definition in real-life cases.

**High-profile mergers**

In June 2017, the JFTC published its annual business combination report looking at the biggest transactions in the fiscal year 2016. That year, two deals in Japan's petroleum refining and wholesale industry were noteworthy—the acquisition of TonenGeneral Sekiyu K.K. by JX Holdings to create Japan's biggest oil refiner and the purchase of Showa Shell Sekiyu K.K. by domestic rival Idemitsu Kosan Co.

The JFTC reviewed approximately 45 relevant markets, including those with high combined shares, such as the LP wholesale gas market of approximately 80–90 per cent.

The JFTC conducted reviews of both transactions in parallel. On 19 December 2016, the JFTC published a press release announcing its decision to grant clearance to both transactions, subject to the remedies proposed by the relevant parties.

These cases are significant because although the notification for the Idemitsu transaction was submitted several months before that of the JX transaction, the JFTC reviewed both transactions together, rather than applying the European Commission's 'first- come, first-served' approach.

# Enforcers take aim at gun-jumping

Gun-jumping has been in the crosshairs of competition-law enforcers for the past decade, and recent developments show authorities across the world are taking an even tougher line

*By Jean-Julien Lemonnier*

Most practitioners classify gun-jumping as a scenario in which the parties to a transaction appropriately send formal notification of the transaction to the relevant competition agency, but then coordinate their activities during the mandatory pre-closing suspensive period. This conduct is referred to as 'substantive gun-jumping', and it usually leads to an intricate approach by competition authorities involving several theories of harm.

Competition enforcers also often look into what is called 'procedural gun-jumping', which is a separate infringement for a complete absence of any filing before the respective authority.

**Why is gun-jumping a trending topic in 2018?**

Gun-jumping has been in the spotlight for the past several years and transaction-driven industries need to be keenly aware of the increasing activism of local and global antitrust enforcers. Recently, both procedural and substantive gun-jumping have been widely sanctioned, with several fines ranging in the millions of euros.

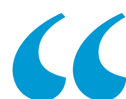
A clear trend can be discerned in cases spanning four continents. In 2016, in North America, the US Department of Justice fined Flakeboard and SierraPine a combined total of close to US$5 million dollars for pre-closing coordination conduct in violation of the Hart-Scott-Rodino and Sherman antitrust acts. The same year in South America, CADE, the Brazilian competition agency, sanctioned Cisco and Technicolor approximately €8 million after having issued gun-jumping guidelines in 2015.

In Asia, MOFCOM, the Chinese competition enforcer, has recently put in place a gun-jumping whistleblower notice and has sanctioned a foreign undertaking (Canon, for its acquisition of Toshiba Medical) ¥300,000 (€38,000 approximately).

In Europe, the Commission recently fined the Norway-based Marine Harvest €20 million (the case was upheld by the General Court and is now pending in the Court of Justice). In April 2018, the Commission imposed a €125 million fine upon Altice for implementing its acquisition of Portugal Telecom (Altice instantaneously announced its intention to lodge an appeal against this decision). Member States including Poland, Romania, Spain, Austria and several others have imposed fines ranging in the hundreds of thousands on local operations.

In addition, the Danish High Court is currently awaiting clarification from the Court of Justice following the referral of a case in relation to the acquisition of KPMG Denmark by EY. In the context of this operation, KPMG Denmark announced the early termination of its cooperation agreement with KPMG. The Danish Competition Authority ruled that by doing so, the companies had jumped the gun. In January 2018, AG Wahl released a (non-binding) opinion in which the standstill obligation does not affect measures that 'precede and are severable from the measures actually leading' to controlling the target undertaking, even if these are taken in connection with the transaction. In a nutshell, AG Wahl considers that ending a cooperation agreement does not violate the gun-jumping prohibition. The judgment of the Court in this case is expected in the coming months.

**4**
Regulators on four continents have recently taken action against gun-jumping

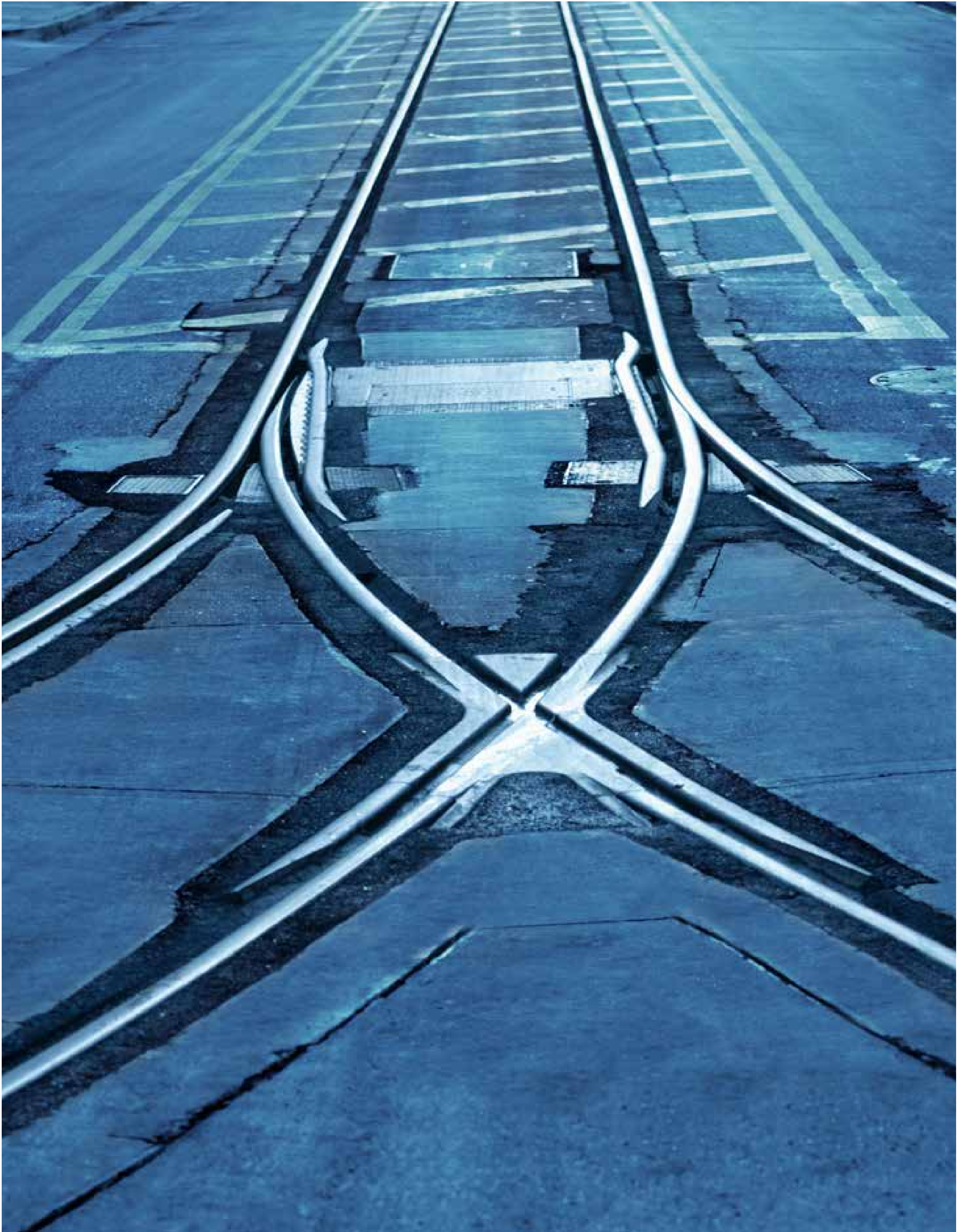


**EU Member States including Poland, Romania, Spain and Austria have imposed fines on local operations**

In France, up until recently, gun-jumping sanctions had only been imposed where there was a complete lack of notification with the national enforcer. However, Altice—which is a full-on substantive gun-jumping case—has been in the spotlight for over a year, raising several questions for future operations.

**Is the Altice case in France indicative of a shift towards a more restrictive stance on pre-clearance conduct?**

The French Competition Authority's (FCA) analysis in the Altice case of November 2016 has been widely discussed by practitioners as it was the first time, at least at the European level, that a gun-jumping decision provided an almost 'catalogue-like' and in-depth assessment of several



types of pre-closing practices. With Altice, the FCA appears to have taken a bold step, imposing, at the time it was rendered, the highest worldwide fine for gun-jumping conduct: €80 million.

There is spirited debate among practitioners as to how to interpret the somewhat restrictive approach of the decision in several key areas, notably information exchange. In particular, as far as information exchange is concerned, the FCA has held that 'whatever the reasons for which the undertakings would need to exchange information, it is incumbent on them to establish a framework which would eliminate all communication of strategic information between independent undertakings in light of the Guidelines on the applicability of Article 101 TFEU [Treaty on the Functioning of the European Union] to horizontal co-operation agreements'. Furthermore, the wording of the decision (here quoted from an English translation of the decision, paragraphs 260 and 318) appears to make it difficult for in-house legal advisers to be included in the deal process. Moreover, it seems that they 'cannot be considered as making possible the avoidance of the dissemination of strategic information between the two undertakings'.

The decision continues: 'As a matter of fact, the two individuals who were the recipients of the commercially sensitive information were the in-house counsels, who are not subject to the same rules of confidentiality applicable to external attorneys … [T]hey are subject to the hierarchic authority of the company and cannot be considered as independent of the company's management. For this reason, it should be considered that their access to commercially sensitive information is equivalent to the entire company obtaining access to the said information.'

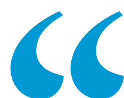
During a March 2017 conference, the FCA attempted to limit the decision's reach by stating that it consists of more of a sui generis decision than a landmark one. However, the decision could have broader implications because this rigid approach taken by the Authority forms part of the body of precedents of its administrative practice and therefore could lead to similar cases in the future.

**What advice should be given to dealmakers in the current regulatory climate?**

In general, caution should be taken towards potential issues related to sale or purchase agreements (SPAs). In particular, the wording of the SPA should not be over-restrictive, granting veto rights over certain types of conduct of the target, which would result in de facto control. On the other hand, the acquirer and the target should not over-interpret the SPA clauses. In Altice, SFR asked for Altice's approval of certain actions without the SPA expressly requiring it, giving the FCA the impression of control.

Information exchange also appears to be a more and more controversial area in merger control, meaning that the composition and internal functioning of 'clean teams' may fall under the scrutiny of competition authorities. Certain confidential information that companies would like to transmit through a 'clean team' is not, in fact, suitable for sharing prior to the merger's closing, and would need to be processed by an independent third party and returned in a non-confidential form.

Joint commercial dealings are another type of conduct that should be handled with caution. The joint conception of future projects during the suspensive period could be flagged by competition agencies. As seen in Altice, the FCA sanctioned a joint project of the acquirer and the target that was conceived during the suspensory period and was launched just days after clearance was granted.



**The joint conception of future projects during the suspensive period could be flagged by competition agencies**

**€125m**

The record-breaking gun-jumping fine levied by the European Commission on Altice

**What can we expect from the road ahead?**

At the time of writing, the Commission's Altice decision is not publicly available. We can expect that it will provide further clarification, especially since some of the conduct appears to be comparable to the French Altice case, particularly the exchange of commercially sensitive information, the intervention in marketing campaigns, and the contents of the covenants in the SPA (particularly, how they are applied by the parties). Likewise, additional criteria may be provided by the Commission (Canon/Toshiba case), and in national competition authorities' decisions, which should be rendered this year.

Finally, in France, following the Altice case, competition law practitioners have asked for some general guidance as regards gun-jumping. The FCA has taken this into consideration and will publish an article providing additional indications of what it considers to be gun-jumping.

# Too late for a fix?

When European Union Courts overrule European Commission decisions on transactions, finding a solution to the situation can be challenging for parties to the deal

*By Jérémie Jourdan, Martin Möllmann*

In 2017, the European Union (EU) General Court annulled two merger decisions of the European Commission. In March, the Court overturned the Commission's 2013 decision to block the proposed €5 billion acquisition by United Parcel Services (UPS) of Dutch delivery group TNT Express NV (TNT). The Court annulled this decision on the basis that the Commission had failed to communicate a final version of its econometric analysis—which had been used in support of its objections—to UPS, breaching UPS's rights of defence.

Then in October, the Court annulled a decision by the Commission to clear the €10 billon acquisition of Dutch cable operator Ziggo by Liberty Global of the US. That decision, taken in 2014, was appealed by a competitor and annulled because it did not sufficiently explain why some of the negative vertical effects raised by this competitor during the administrative procedure could be excluded. As a result, the parties had to re-notify the transaction and the Commission to re-examine it under market conditions applicable at the time of re-notification.

Such annulments are rare. EU Courts had previously annulled only eight Commission decisions under the Merger Regulation over a span of 25 years. Annulments of clearances are even rarer, with only four precedents: Kali und Salz/MdK/Treuhand; RAG/Saarbergwerke/Preussag; SEB/Moulinex; and Sony/BMG. Both recent cases, however, illustrate the challenges of judicial review of merger decisions.

**Annulment of prohibition decisions**

When prohibition decisions are annulled, there is no guarantee that winning the court battle will be sufficient to save the deal, nor does it automatically mean that the Commission was wrong to prohibit a transaction.

The prohibition by the Commission of the 2001 merger between French industrial groups Schneider and Legrand (Schneider/Legrand), in which the Commission was faulted for a breach of the rights of defence, was annulled. But after the annulment, the Commission confirmed its suspicion that the transaction would raise competition issues. As a result, Schneider decided to sell Legrand (which had already been acquired by means of a public exchange offer).

Sometimes, there is actually nothing to be fixed. For example, UPS's recent victory will not allow it to win its prize: Its main rival, FedEx, acquired TNT in the meantime. What is left is the possibility to seek damages. At the time of writing, UPS had filed an action before the General Court seeking US$2.1 billion in damages. However, such damages are notoriously difficult to obtain and generally of a very limited amount. In Schneider/Legrand, the Court of Justice merely granted damages of €50,000 for expenses incurred by Schneider in relation to the re-examination of the merger.

**€10bn**

A rare annulment saw Liberty Global and Ziggo re-notify a merger transaction to the European Commission

There are cases that have had a positive outcome for the parties involved. For example, Sweden's Tetra Laval eventually obtained clearance for its €1.6 billion acquisition of French packaging equipment maker Sidel following the annulment of the Commission's initial prohibition. In that case, the Commission decision was annulled by the Court for failure to meet the burden of proof. On its second attempt, the Commission found that the standard set out by the Court for prohibiting a merger because of risks of tacit collusion was not met. It then cleared the merger.

**Clearance appeals**

When a clearance decision is successfully appealed by a third party, the acquirer faces a risk of seeing the corporate integration being called into question years after its implementation. The parties must submit a new notification and the Commission has to take a fresh decision in light of current market conditions. This process, known as 're-adoption', can be lengthy and potentially cause the Commission to impose new remedies, or even to prohibit the transaction.

**When prohibition decisions are annulled, there is no guarantee that winning the court battle will save the deal**

This can give rise to considerable complexity. After the European Commission's decision cleared the proposed merger between Sony and Bertelsmann in 2004, a third party successfully challenged the ruling before the General Court. The Commission then cleared the transaction again. In parallel, the merging parties successfully appealed the General Court's judgment before the Court of Justice. But in the meantime, the same third party who had challenged the first decision also appealed the second clearance decision. Sony eventually acquired sole control of the joint venture, leading to the closing of the pending appeals as they had become devoid of purpose.

**Expedited action**

It is essential that EU courts decide on Commission merger decisions as quickly as possible. The parties should therefore apply for an expedited procedure when appealing a prohibition decision. This will allow a priority treatment and a shorter written phase, usually with only one round of written submissions, and a shorter deadline for the defendant to file its submission.

In four previous cases of annullments of Commission decisions, the General Court granted the expedited procedure when the parties requested it and ruled within a period of between nine and 19 months. The request was, however, refused in the UPS/TNT case when the General Court's review turned out to be particularly lengthy (four years), which was surprising given that the proceedings ultimately led to a short judgment, annulling the decision on a procedural ground.

In the Liberty Global/Ziggo case, neither the third party appealing the decision nor the Commission requested an expedited procedure. Because of the Court's rules of procedure, the one that really had an interest in such expedited treatment— namely Liberty Global— had no right to request it, even if it had intervened in the case (which it had not). And an intervention by Liberty Global in the case would have likely slowed down proceedings even more. As regards possible mitigating strategies, if the parties to a transaction cleared by the Commission suspect that a third party might appeal that decision, they can try to safeguard their interests by, first, trying to accelerate the publication of the Commission decision. They can do this by submitting confidentiality requests on the decision as soon as possible in order not to delay the publication of the non-confidential version (the clock for third parties to appeal the decision starts ticking when the non-confidential version is published). Likewise, during the court proceedings, they will be asked to submit a confidentiality request, and may accelerate proceedings by not making unduly broad confidentiality requests. Finally, if they believe that there is a material risk of full or partial annulment of the clearance decision, they could take ring-fencing measures in order to facilitate the unscrambling of the eggs, should they eventually have to divest part of the target business.

**Sometimes there is nothing to be fixed. For example, UPS's recent victory will not allow it to win its prize**

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