Merger Control

First Edition
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Published by Global Legal Group

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Overview of merger control activity during the last 12 months

In July 2011, the German Federal Cartel Office ("**FCO**") published its biannual activity report for 2009/2010.[i] In 2010 a total of 987 transactions were notified to the FCO, of which 62 transactions were not considered to be subject to merger control under sections 35 *et seq.* of the German Act against Restraints of Competition ("**ARC**"). The number of transactions cleared in Phase I, i.e. within one month after the notification is deemed to be complete by the FCO, amounted to 879. Only 15 transactions were examined by the FCO in Phase II proceedings, i.e. within four months upon the receipt of a complete notification, of which six transactions were cleared without any conditions, three were conditionally cleared and only one was prohibited. In the remaining five Phase II cases, the parties withdrew their notifications.

Whereas in comparison to 2009 with an overall number of 998 notified transactions the number of notifications remained on more or less the same level, the amount of notifications reduced by approx. 40% in comparison to 2008 when an overall number of 1,675 notifications were made and even by approx. 55% in comparison to 2007 with an overall number of 2,242 notified transactions. It can be assumed that, apart from the economic crisis in 2009, this development is certainly a result of a second domestic threshold of EUR 5 million, which was introduced in March 2009. Since then, a concentration in the sense of section 37 ARC has to be notified to the FCO if:

- the relevant parties in the last completed financial year preceding the transaction achieved a combined aggregate worldwide turnover of more than EUR 500 million; and
- at least one party had a turnover of more than EUR 25 million in Germany; and
- the domestic turnover in Germany of another party exceeded EUR 5 million.[ii]

The ARC also provides for two exemptions from the filing requirement, which apply under the following conditions:

- one party to the merger had a worldwide turnover of less than EUR 10 million in the last completed business year preceding the transaction; or
- on the relevant market, which must have existed for at least five years, the total turnover achieved by all market participants in Germany amounted to less than EUR 15 million (so-called *de minimis* market).

However, with regard to the *de minimis* market exemption, it should be noted that the FCO under certain conditions may also bundle neighbouring markets in order to determine the overall size of the relevant market in the sense of the ARC. Hence, the second exemption is only applicable for a rather negligible number of mergers.

New developments in jurisdictional assessment or procedure

In its activity report 2009/2010 the FCO clarified a number of controversial legal issues.

With regard to joint ventures, the introduction of the second domestic turnover threshold leads to the question of whether the turnover of the joint venture has to be fully allocated to both the joint venture itself and the parent companies. The FCO stated that such a double turnover allocation would not be appropriate and would not reflect the factual economic importance of the transaction.

In relation to the turnover allocation in the banking sector, the FCO now clarified that, in accordance with Art. 5 para 3 of the EC Merger Regulation ("**ECMR**"), the turnover of a credit or a financial institution should be allocated to the branch or division of that institution and not to the location of the customer.

Concerning the outsourcing merger notifications, the FCO abandoned its administrative policy established in the activity report 1995/1996 according to which outsourcing asset mergers did not have to be notified to the FCO if the relevant turnover achieved by the assets amounted to less than EUR 5 million in the last completed financial year preceding the transaction.[iii] Due to the significantly increasing volume of such mergers in the last 15 years and the adoption of the second domestic turnover threshold of EUR 5 million the FCO is now of the view that the exemption has to be revoked. In future, such asset outsourcing transactions will be judged under general merger control rules.

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Key industry sectors reviewed, and approach adopted, to market definition, barriers to entry, nature of international competition etc.

In 2010 and 2011, FCO's scrutiny *inter alia* focused on merger control notifications in the food retail sector. In some merger cases over the past couple of years, the FCO was of the view that the major German food retail chains hold a very strong position *vis-à-vis* their suppliers in the respective procurement markets. In its merger decision with regard to the acquisition of the beverage supplier, Trinkgut, by one of the largest food retails chains, EDEKA, in October 2010, the FCO considered that EDEKA, REWE and the Schwarz Group (the latter including Kaufland and Lidl) could constitute a potential oligopoly in relation to beverage suppliers (according to the FCO's findings, the fourth largest German retail chain in the food sector, Aldi, held only a minor market share in the relevant beverage procurement market). Due to the significant competition concerns, the FCO finally cleared the merger after an in-depth analysis in Phase II subject to conditions to be fulfilled by the parties prior to implementing the merger.[iv] In the merger case between EDEKA and another food retail chain, RATIO, in 2010, the parties even had to withdraw their initial merger notification after the FCO indicated that the notified merger would lead to significant competition concerns.[v] Therefore, the parties had to exclude problematic regional markets from the transaction scope and notified the transaction again which was then cleared by the FCO without any conditions already in Phase I.

In addition to the very close analysis of the respective merger notification, the FCO has also launched a sector inquiry into the food retail sector in February 2011. The FCO's sector inquiry focuses on the competitive conditions in the markets for the procurement of food and luxury food products by food retailers. The FCO is of the view that the increasing consolidation in the food retail sector leads to a high level of concentration in favour of the leading trading companies not only in the sales markets, but also in the procurement markets. The four leading retail companies, EDEKA, REWE, the Schwarz Group and Aldi, control approx. 85% of the total sales market in Germany. The FCO intends to use the investigation to support its previous analyses of the procurement markets in the food retail sector. The scope of the sector inquiry will be narrowed to specific individual questions, such as the examination of positions held by the individual retail companies in the procurement of goods on the basis of selected product groups. The FCO aims at determining whether and to what extent the leading food retailers enjoy purchasing advantages over their competitors. In addition, the FCO will also analyse the effects of such advantages on competition in the sales markets.[vi]

Apart from the food retail sector, the FCO continued to follow its rather strict approach with regard to mergers in the TV broadcasting sector. In 2011, the FCO prohibited a proposed joint venture between Germany's largest private broadcasters RTL and ProSiebenSat.1 to create an internet platform for catch-up television on demand. The purpose of the joint venture was to create a central online platform on which consumers could watch television programmes aired in Germany and Austria up to seven days after their initial broadcast on television.[vii] Initially, the parties notified the joint venture to the European Commission. However, the Commission referred the case to the FCO and the Austrian competition authority upon the respective requests. The FCO was of the view that the joint platform would have further strengthened the existing dominant duopoly between the two broadcasting groups on the market for TV advertising. Therefore, the FCO requested RTL and ProSiebenSat.1 to open the platform to third parties and broadcasters and to lift the restrictions on the time of availability and quality of content. However, RTL and ProSiebenSat1 refused to accept such changes to the original concept of the joint venture which lead to the prohibition of the transaction.

With regard to the fuel sector, the FCO published the results of its respective sector inquiry on 26 May 2011.[viii] The sector inquiry was launched in May 2008 following antitrust concerns about high price levels at German petrol stations. In the course of the inquiry, the FCO representatively collected and evaluated data on all price changes from 1 January 2007 to 30 June 2010 at more than 400 petrol stations in Hamburg, Cologne, Leipzig and Munich. In its final report the FCO stated that the five largest petrol station operators in Germany, Aral, Jet, Esso, Shell and Total, form an oligopoly on the relevant market in Germany accounting for approx. 65% of fuel sales. According to the FCO's findings, the transparency of the fuel market and, in particular, the use of monitoring systems, enabled the oligopoly members to quickly react to any price changes initiated by other market players. Additionally, the FCO considered that the oligopoly members followed certain price-setting patterns enabling them to set the fuel prices more or less uniformly. Finally, the inquiry also revealed numerous links between the oil companies making it difficult for members to break away from the oligopoly. However, as a conclusion, the FCO found that there are no anti-competitive agreements between the oligopoly members due to the particular market structure which as such leads to higher prices without necessarily requiring anti-competitive agreements between the oligopoly members. In this respect, it should be additionally noted that in one of its recent rulings relating to the fuel sector, the Higher Regional Court in Düsseldorf did not support the FCO's conclusions with regard to the oligopolistic structure of the market and overruled the FCO's prohibition decision with regard to the acquisition of 59 gas stations by Total from OMV in Eastern Germany.

Approach to remedies (i) to avoid second stage investigation and (ii) following second stage investigation

FCO's approach to remedies generally depends on the stage of the merger investigation. As mentioned above, in Phase I the FCO has one month to examine a notified transaction after the FCO deems the notification to be complete. If a Phase II investigation is conducted, the waiting period is four months from receipt of a complete notification and may additionally

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be extended with the consent of all notifying parties. A notified merger is deemed to be cleared if the FCO fails to issue a decision within the period set for Phase I and/or Phase II. In general, the ARC does not provide for any tools to "freeze" the clock. However, the parties can generally reset the clock by withdrawing and re-filing the notification.

When examining a notified merger the FCO can approve the transaction, prohibit it or clear it subject to conditions and obligations. Before prohibiting a merger or imposing clearance conditions or obligations, the FCO is obliged to inform the parties about the reasons for its decision in order to give them the opportunity to argue against the FCO's statement of objections and/or to offer remedies. The latter is, however, only possible in Phase II proceedings. In Phase I there is, however, the possibility to discuss with the FCO under which circumstances (i.e. changes to a transaction) it would grant a clearance letter within the initial one-month period. If a "remedy" was found, the parties could withdraw the filing and file the transaction again, however, in the new/agreed form.

Under the current ARC, the FCO expects to be offered only structural remedies, e.g. the sale of a particular business or shareholding, rather than behavioural remedies, e.g. third parties' supply obligations. With regard to the time frame, there is no particular legal deadline to offer the remedies. However, if the parties offer the remedies at a rather late stage of the investigation process, the FCO may require an extension of its review period. Generally, if a structural remedy has been accepted by a competition authority in another jurisdiction, the FCO will tend to consider such remedies. However, the FCO will probably not waive its request for a formal remedy offer. In addition, it should be noted that the remedies offered might be tested by the FCO with other market participants or third parties that have been admitted to the examination proceedings.

From a procedural point of view, the FCO mostly used subsequent orders to enforce the remedies offered, i.e. the parties could first complete the transaction and then comply with the conditions agreed upon with the FCO. If the parties failed to fulfil the conditions in the agreed time frame, the clearance decision automatically turned into a prohibition of the merger. However, it now seems that the FCO has changed its administrative practice in this respect. In a number of recent cases, commitments were included by way of a condition precedent meaning that the parties could not close the envisaged merger prior to fulfilling the obligation. This approach leads to a number of problems for the parties, e.g. voidness of contracts, in particular if the parties cannot complete the notified merger for a relatively long time. Apart from the voidness of the agreements the parties may also face significant fines if they infringe the completion prohibition. In two cases in 2008[ix] and 2009[x] the FCO imposed fines of approx. EUR 4 million each. In 2011[xi] two other decisions were issued in which the FCO sanctioned the violation of the completion prohibition. For the sake of completeness, it should be noted that the ARC contains in section 41 para 2 ARC a provision according to which the FCO may – at least in theory – grant exemptions from the prohibition of putting a concentration into effect if the undertakings concerned put forward important reasons, in particular to prevent serious damage to a participating party. However, the chances that the FCO will grant such an exemption are in general relatively low.

Key policy developments

On 21 July 2011, the FCO published "Draft Guidance on Substantive Merger Control" which is the first substantial overhaul to the application of merger rules for more than a decade.[xii] The draft is subject to a public consultation procedure and is expected to be published in its final version in autumn 2011.

In contrast to the previous guidance document on the "Principles of Interpretation of Market Dominance", the new draft places greater emphasis on the necessary appraisal of all relevant conditions in the market and examines how the merger will change market conditions and whether this will be harmful to competition. In the light of the upcoming amendments of the ARC (see further below) a particular focus of the discussion is whether the prohibition criterion under German merger control rules should be harmonised with the ECMR. If that was the case, the SIEC test ("significant impediment to effective competition") would replace the current dominance test laid down in section 36 para 1 ARC. However, it should be noted that whether a merger would create or strengthen a dominant position would still remain the main example for the SIEC test, i.e. the FCO could apply the vast majority of its established decision practice.

The purpose of the draft is to provide guidance to companies and their legal or economic advisers as to how they can better predict which issues the FCO will be likely to focus on in its appraisal. However, it should be noted that the draft guidance does not contain a check list for a straight-forward assessment, i.e. the companies would still have to conduct a thorough analysis on a case-by-case basis.

Reform proposals

On 1 August 2011, the German Ministry of Economics and Technology published a key issue paper which will be the basis for the so-called "8th ARC Novel" expected to come into force on 1 January 2013. According to the paper, the Federal Ministry of Economics and Technology does not intend to completely overhaul the ARC. However, some of the envisaged changes might have a significant impact on the German merger control practice. The proposed changes include the following issues:

- As already indicated above, the substantive dominance test will be replaced by the SIEC test, i.e. the prohibition criterion to be applied by the FCO would be the same as under the ECMR.

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- The market share thresholds at which market dominance is presumed under the ARC will be increased. Currently, under section 19 para 3 ARC an undertaking is presumed to be market dominant (monopoly presumption) if it has a market share of at least one third. A number of undertakings is presumed to be market dominant (oligopoly presumption) if it:
  - consists of three or fewer undertakings reaching a combined market share of 50%; or
  - consists of five or fewer undertakings reaching a combined market share of two thirds.

  In comparison to the European Commission's decision practice according to which market dominance of a single undertaking is generally presumed at 50%, the dominance market share thresholds under the ARC are rather low. Albeit, the key paper does not contain any exact thresholds to be adopted, a harmonisation with the European Commission's decision practice would certainly lead to more legal certainty and consistency in this respect.
- The FCO considers to accept behavioural commitments in the context of Phase II proceedings. As described above, the current administrative practice of the FCO allows only structural commitments.
- According to a statement of the Monopoly Commission (an independent advisory body of the German Federal Government established under sections 44 ARC *et seq.*) in its XVIII. Biannual Report published on 14 July 2010,[xiii] there is a risk that the second domestic turnover threshold may be circumvented by the parties by artificially splitting the transactions into smaller parts in order not to meet the relevant turnover thresholds. As a risk mitigating tool it is intended to adopt a provision similar to Art. 5 para 2 sentence 2 ECMR according to which two or more transactions within a two-year period between the same persons or undertakings are treated as one and the same concentration.
- Under ARC section 41 para 1 sentence 2 ARC a transaction which has been implemented prior to obtaining a respective clearance decision is void. Under the previous administrative practice of the FCO, the voidness could be healed by a subsequent clearance from the FCO. However, in 2008 the FCO changed its administrative practice in this respect and now refuses to issue such *ex-post* clearance decisions even in cases in which the transaction does not lead to any competitive concerns. Instead, the FCO launches a de-concentration proceeding which is closed if the transaction does not lead to any competition concerns. However, the closing of the de-concentration proceeding is not equivalent to a clearance decision. Hence, in the absence of a clearance decision, there is a degree of legal uncertainty in relation to the validity of the respective agreements. This uncertainty is intended to be resolved by a respective provision in the ARC.
- Under Art. 7 para 2 ECMR the implementation of a public bid is possible prior to receiving a respective clearance decision from the European Commission. The ARC does not contain such an exemption for public tenders. Considering that a notification is usually published on the FCO's homepage, this may lead to implications in particular with regard to confidentiality issues. Currently, this aspect has to be negotiated with the relevant panels on a case-by-case basis. However, the Federal Ministry of Economics and Technology intends to resolve this issue by adopting a respective provision in section 41 para 1 ARC.
- As described above, under section 35 para 1 sentence 2 ARC transactions in which the parties meet the relevant turnover thresholds do not have to be notified to the FCO if the transaction affects a market in which goods or commercial services have been offered for at least five years and in which sales of less than EUR 15 million were generated in the preceding financial year by all companies active on this market. The geographic scope of such a de-minimis market was the subject of a controversial debate in the recent past. The German Federal Court of Justice established that the scope of the de-minimis market is limited to Germany or relevant parts thereof.[xiv] However, according to the so-called bundling theory, the turnover on neighbouring markets in Germany would have to be added under certain conditions. Having said that, the exact details of the bundling theory are still unclear. Therefore, the Federal Ministry of Economics and Technology intends to re-shift the *de minimis* market exemption from formal to substantive merger control as it was the case before the 6th ARC Novel in 1998. If that was the case, a transaction would need to be notified to the FCO even if only a *de minimis* market was concerned. However, if the FCO during its substantive assessment came to the conclusion that a *de minimis* market is concerned it could not prohibit the transaction irrespective of competition concerns.
- With regard to the harmonisation of the ARC with the European competition law provisions, the Federal Ministry of Economics and Technology intends to include additional unbundling powers for the FCO into section 32 para 2 ARC similarly to Art. 7 para 1 of the Regulation 1/2003.

* * *

Endnotes

i. Available on the FCO's website at www.bundeskartellamt.de/wDeutsch/publikationen/Taetigkeitsbericht.php.
ii. For certain industries, e.g. media, banking and retails sectors, the ARC provides for different turnover thresholds.
iii. Outsourcing share deal transactions were never subject to the exemption and were always judged under general merger control rules.

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iv. Case B2-52/10, available on the FCO's website at www.bundeskartellamt.de/wDeutsch/archiv/EntschFusArchiv/2010/EntschFusion.php.
v. Case B2-125/10, available at www.bundeskartellamt.de/wDeutsch/entscheidungen/fusionskontrolle/kurzberichtfus/KurzberichteFusionW3DnavidW2676.php.
vi. The respective press release is available at www.bundeskartellamt.de/wDeutsch/aktuelles/presse/2011_02_14.php.
vii. Available on the FCO's website at www.bundeskartellamt.de/wDeutsch/aktuelles/presse/2011_03_18.php.
viii. The full report is available on the FCO's website at www.bundeskartellamt.de/wDeutsch/publikationen/Sektoruntersuchung.php.
ix. Available on the FCO's website at www.bundeskartellamt.de/wDeutsch/archiv/PressemeldArchiv/2008/2008_12_15.php.
x. Available on the FCO's website at www.bundeskartellamt.de/wDeutsch/archiv/PressemeldArchiv/2009/2009_02_13.php.
xi. Available on the FCO's website at www.bundeskartellamt.de/wDeutsch/aktuelles/presse/2011_01_28.php and www.bundeskartellamt.de/wDeutsch/aktuelles/presse/2011_05_10.php.
xii. Available on the FCO's website at www.bundeskartellamt.de/wDeutsch/merkblaetter/Fusionskontrolle/Ankuendigung_Konsultation_Leitlnien_2011.php.
xiii. Available on Monopoly Commission's website at www.monopolkommission.de/aktuell_hg18.html.
xiv. *Cf.* BGH WuW DE-R 21 33 *et seq.* – Sulzer/Kelmix.

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