

Position paper (translation)

European Commission consultation on procedural and jurisdictional aspects of EU merger control

A. Introduction

The European Commission launched a consultation on certain aspects of EU merger control on 7 October 2016. The focus is on the jurisdictional thresholds and referral system contained in the EU merger control regulation (EUMR) as well as on the simplified procedure. The Federation of German Industries (BDI) sets out below its position on the questions asked in the consultation. We were also involved in the public discussions on the revision of EUMR in 2013 and 2014.

BDI endorses the Commission's intention of organising EU merger control more effectively. We therefore welcome procedural simplifications for mergers which do not raise competition concerns as well as simplifications and streamlining for case referrals. The one-stop shop for European merger control should be extended to Norway, Switzerland and also to the United Kingdom – once Brexit is complete.

In BDI's view, the envisaged introduction of a new, additional jurisdictional threshold would be unnecessary and a wrong turning from the angle of competition. With a jurisdictional threshold linked to transaction size, the European Commission could in future also investigate cases which exhibit no or only very little association with the European Economic Area (absence of "local nexus"). Given that there is just one supposed case repeatedly cited as a precedent (Facebook/WhatsApp in 2014) and without any evident need in the interest of competition, such an increase in administrative effort is unacceptable for companies.

B. Simplification of the procedure

The consultation invites comments as to whether a simplification of the merger control procedure could be achieved, e.g. through a widening of or changes to the simplified procedure or by excluding certain, non-problematic transactions from the Commission's area of competence.

- *No notification requirement for certain transactions*

BDI favours the introduction of a local nexus requirement in relation to the notification obligations for joint ventures in order to ensure that transactions only trigger a formal obligation to notify the Commission if the joint venture itself (and not its parent companies) is active in the EEA or there are firm plans for the joint venture to become active in the EEA in the near future.

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**Federation of German
Industries**
Member Association of
BUSINESSEUROPE

T: +3227921005
F: +3227921030

Internet
www.bdi.eu

E-Mail

N.Rossmann@bdi.eu

If the agreements underpinning the creation of the joint venture clearly limit its geographical area of activity to an area outside the EEA and if the shareholders' roll-out plans also do not foresee any imminent extension of the joint venture's activities into the EEA, there is no logical reason for regulatory control by the EU. The mere fact that parent companies reach EUMR threshold values does not justify such events being subject to EU merger control. In this area, the German Federal Cartel Office has now adopted a more flexible approach with its "Guidance on domestic effects in merger control". Other competition authorities (e.g. CADE) are also proving to be more flexible in practice. ECJ's Gencor jurisprudence often advanced for EU law in this connection is not appropriate. It is also important not to underestimate the negative example set by EUMR for less experienced competition law orders which additionally often still have low jurisdictional thresholds. This constitutes a considerable obstacle for many M&A transactions – also due to suspensive effects to be observed – leading to unnecessary formalities and increased transaction costs.

Similarly, BDI believes that an exemption from the formal notification obligation should be made for transactions in which there are no horizontal overlaps and no substantive vertical relations between the companies involved or the subject of the notification would be a mere change from joint control to single control.

Written information on the merger to the Commission should be sufficient for such transactions, with a possibility for the Commission either to allow the merger within ten working days or to demand a formal notification in the simplified procedure.

- ***Improvements to the simplified procedure***

Overall, it can be observed that the "simplified procedure" has demonstrated positive effects by somewhat reducing the time effort, the necessary resources as well as the costs of a notification. However, despite this very helpful simplification, the effort required of companies involved is still considerable. This applies in particular for the internal documentation to be submitted. The pre-notification procedure and requests for information ("RFIs") could be optimised. Furthermore, a procedural simplification would be desirable also for mergers completed without the benefit of the simplified procedure.

It would be helpful if the case team could discuss with the parties to a transaction, at the start of the pre-notification phase, the timetable as well as the planned focus and reach of the investigation by the Commission and the data and information available to the parties.

The range of information requested by the Commission exceeds the range of documents requested by national authorities and often leads to long-winded processes. The very short response periods are problematic in this connection. The requested market data are often not directly available but have to be collected or estimated individually, leading to a considerable effort in terms of personnel and time. This is the case, for example, if a company's administration only has figures on individual national markets but the Commission's geographical market delimitation encompasses purely local or cross-border markets. Longer response periods and a streamlining of the RFIs should be envisaged. Moreover, a

limitation of the scope of the RFIs to information which is absolutely necessary for evaluation of the transaction would be desirable to keep the effort for companies within reasonable bounds. This applies in particular for cases which are obviously non-critical. It should be ensured that the questions are unambiguous, specific and tailored to the party in question. To the extent possible, RFIs should be combined and consolidated.

Where internal documents are requested, it should be ensured that these requests are sufficiently specific and restricted to the necessary information. Should an extensive data query be necessary, this should ideally be submitted during pre-notification.

Furthermore, pre-notification should be used to exclude themes which in all probability will not lead to relevant competition concerns before the Commission's investigation even starts.

In addition, it would be desirable if greater flexibility in the presentation of data were given, in particular when large volumes of data are requested.

- ***Self-assessment system***

BDI believes that a self-assessment system for certain categories of cases as proposed in the Commission's questionnaire deserves consideration. In the interest of legal certainty, it would be important in the event of such a system that the European Commission issues accompanying guidelines which identify in concrete terms the categories of case where a notification can be dispensed with and the cases where a notification is absolutely essential. Here, too, we refer just by way of example to the German Federal Cartel Office's Guidance on domestic effects in merger control.

According to the questionnaire, a self-assessment system would be associated with the Commission's right to carry out an ex-post investigation. In the interest of legal and transaction certainty, this investigation right would have to be clearly restricted to cases with an evident legal relevance. For this, too, corresponding guidance from the Commission in the form of guidelines or a communication would be necessary. If the risks of a self-assessment (ex-post ban including an unbundling order, ex-post conditions or fines, etc.) are too high, this would lead to a large number of precautionary notifications. That in turn would run completely counter to the idea of a self-assessment system and to the desired procedural simplification.

C. Notification thresholds

The European Commission takes up in its consultation the question currently much discussed of whether the European model of turnover-based notification thresholds is still of the moment or whether, in the light of takeover cases such as Facebook/WhatsApp, a new jurisdictional threshold is necessary for cases where a company may not (yet) have any significant turnover in the European Economic Area but nevertheless has a considerable market potential which is supposedly expressed in a high purchase price. The digital economy and pharmaceuticals industry are mentioned as sectors particularly affected.

A comparable discussion is currently being held in Germany. The government draft of the 9th amendment to the German law against competition restrictions (GWB) published on 28 September 2016 makes provision in its § 35 paragraph 1a for a new jurisdictional threshold in merger control. The German Federal Government proposes that mergers where the consideration exceeds € 400 million must in future be notified, even if a company has no turnover on the German market. Alongside the turnover threshold in § 35 paragraph 1 point 1 of the proposal, the only condition for a notification is that the company has a turnover of more than € 25 million in Germany and that the acquiring company should be active in Germany “to a considerable extent”.

BDI rejects the introduction of a new notification threshold linked to the consideration or transaction volume as unnecessary and a wrong turning for competition policy. Any extension of the notification thresholds which would automatically lead to higher administrative burdens on companies runs counter to the European Commission’s central objective of simplifying the EU merger control system. For these reasons, there has also in recent years been considerable criticism of the Commission’s plans, now set aside, to extend merger control to non-controlling minority shareholdings.

A new notification threshold that is calculated on the basis of the transaction size jeopardises the principle of “local nexus” in merger control and leads to an increase in administrative effort for companies without any need being evident in the interest of competition. The result could be an inconsistent mixture of the EU system triggering notification based on turnover-based thresholds and the US system (“size of transaction”), due to a single supposed precedent (Facebook/WhatsApp).

It can be assumed that such a change to the jurisdictional thresholds would then act as an example for other jurisdictions. This would lead to overlapping and very unwieldy test procedures not only for companies but also for antitrust authorities, both of which already have only limited human resources.

The Commission asks the right critical questions in its consultation: is there in fact a regulatory gap which would make a change to the current system necessary? If a new threshold is introduced, how can it be ensured that no unnecessary administrative burdens are created for companies? How can it be ensured that only transactions with implications for competition in the European Economic Area are captured by the European Commission’s notification obligation (“local nexus”)? The Commission should also find the right critical answers to these questions and only take action if it can be demonstrated on the basis of empirical studies and statistically significant data that there really is a gap in the system which needs to be closed at European level. In the eyes of German business, no such gap in the system exists.

- ***No gap in the system – but high costs for companies***

A gap in the system would presuppose that there is a significant number of M&A transactions each year which have not hitherto been subject to notification because the turnovers were too low but which nevertheless have an impact on competition in the European Economic Area (EEA) and should therefore have

been investigated in advance by the European Commission. Yet such a significant number of M&A transactions is not evident. The repeatedly mentioned Facebook/WhatsApp case on its own is not sufficient to justify structural changes in merger control to the extent envisaged. Furthermore, this takeover was ultimately investigated by the European Commission anyway thanks to the referral system and approved without undertakings in phase 1. This also argues against a regulatory gap and shows that the current system of EU merger control with its turnover-based jurisdictional thresholds functions. Other “loophole cases” are not known, neither in the digital economy and pharmaceuticals industry as discussed in the consultation nor in other economic sectors. Hence, there is no gap in the system justifying legislative action on the basis of the existing facts.

An extension of EU merger control would lead to an increased administrative effort and an additional cost factor for companies. First of all, markedly more and in particular non-problematic cases would be captured by merger control in the EU. In addition, there is a possibility that companies would consult the Commission with questions relating to a possible notification obligation or notify their mergers by way of precaution. This is associated not only with high external legal advice costs but also with costs through the high in-house effort for examination, collection of data, restriction and diversion of business during and as a result of an ongoing merger control procedure, time delays in completion of the transaction, etc.

In addition, a new jurisdictional threshold based on transaction size would also lead to a clearly increased time and financial effort for the Commission and extend the Commission’s scarce resources to cases which in all probability do not justify any official measures in the EU. This should be seen in a critical light against the background that the European Commission’s resources are limited anyway. Accordingly, these resources should be prioritised and deployed for cases which genuinely have competition implications within the EEA.

- ***Deletion of local nexus principle***

The market relevance of the acquisition of a company which operates partially or completely free of charge is always a question of the total turnover of the company in question and not of its turnover in the EEA alone. Only when the global turnover of the target company is set against the total value of the transaction can a possible discrepancy be established. Sacrificing the turnover threshold rule to address this means justifying a jurisdiction for the Commission for transactions with little or no relevant turnover in Europe but with a relatively high purchase price.

There is a danger that the local nexus principle which is also upheld by ICN and is enshrined in the latter’s Recommended Practices will be abandoned in Europe through the introduction of a jurisdictional threshold based on transaction size. Such a jurisdictional threshold offers an insufficient guarantee that there is an adequate local nexus and that implications for competition in the EEA can be expected. This would in future lead to a notification obligation in many cases where no competition implications for the EEA can be expected. In particular, large international transactions with little or no EEA impact would fall under European merger control in this way.

Especially against the background that most countries have now introduced merger control regimes, there is no reason why an individual jurisdiction should draw a large number of transactions with minimal or no local nexus into their merger control. Rather, it would and should be possible to rely on those jurisdictions where there is an important local nexus to address competition problems or reservations arising from transactions and which are detrimental to or have an impact on supranational markets.

The Commission proposes in its consultation as a possible solution that takeovers should be investigated at EU level only “if they are likely to produce a measurable impact within the EEA”. This criterion is much too vague to offer companies legal certainty and avoid unnecessary notifications. Not only is it unclear when a “measurable impact” can be assumed – neither is the forward-looking prognosis (“if they are likely”) conducive to a legally certain decision on whether to undertake a notification. The Commission announces that there would be more detailed explanations around this criterion. But very high requirements would then have to be placed on these explanations so that a clear decision can be taken on when a takeover can be expected to have a “measurable impact”. A few sample cases as currently found in the explanatory memorandum of the German draft law – which chooses a similarly vague formulation with the criterion of domestic activity “to a considerable extent” – would be insufficient here.

In addition, the proposal recalls the override situation of “considerable influence on competition” (§ 37 paragraph 1 point 4 GWB) in German law which has led to an over-regulation which goes far beyond the objective of deterring restrictions of competition and places heavy burdens on companies. Under the yardstick of this provision, mergers which could potentially have a “considerable influence on competition” are also captured (risk situation). Despite many years of practice with application of this criterion, the concept of “considerable influence on competition” has lost little of its lack of clarity and imprecision. The associated legal uncertainty and the considerable sanctions in the event of failure to notify eligible cases have intensified the pressure on companies to notify their mergers by way of precaution, if there is the slightest doubt that this merger criterion is met. Uncertainty in practical application of the law has tended to lead towards a progressive lowering of the threshold above which a merger is notified – even if only for reasons of legal caution. The administrative effort for companies due to the notification obligation is considerable and is disproportionate to antitrust authorities’ control and investigation possibilities. It is therefore certainly not to be recommended that the EU takes over a similarly vague provision as this criterion of German law. This is all the more the case because the effort involved in a notification at European level is far greater than it is before the German Federal Cartel Office.

Insofar as the European Commission decides in favour of a new jurisdictional threshold despite the criticisms set out above, it must therefore be ensured – specifically for M&A transactions outside the EEA – that a new jurisdictional threshold only captures mergers which impact on competition in the EEA and hence have a sufficient local nexus. For instance, the existence of a sufficient impact on the EEA could be verified against a transaction value allocated to the EEA or against the value of assets acquired in the EEA and/or the value of shares acquired in the EEA or other ownership rights in the target company.

The American “size of transaction test” often cited in the discussion as an example also provides for a clear domestic connection. In the USA, the restriction to the notification obligation to mergers which have an impact on competition in the USA and accordingly have a local nexus is ensured by additional preconditions whereby “acquisitions of foreign assets or voting securities of foreign issuers” (16 C.F.R. §§ 802.50 and 802.51) are eligible only if the foreign assets the acquiring person would hold as a result of the acquisition generated sales in or into the U.S. exceeding (currently) USD 78.2 million during the acquired person's most recent fiscal year or if the issuer either holds assets located in the United States having an aggregate total value of (currently) over USD 78.2 million or made aggregate sales in or into the United States of (currently) over USD 78.2 million in its most recent fiscal year.

The threshold values are markedly higher for “foreign to foreign transactions”. Hence, turnover figures and balance sheet totals in the USA of the parties to the merger play a decisive role in determining whether there is a notification obligation for a transaction in the USA. These additional threshold values for turnovers and assets supplementing the jurisdictional threshold based on transaction size ensure that no transaction which does not have an important local nexus in the USA triggers a notification obligation in the USA.

Moreover, in the event of a jurisdictional threshold based on transaction size being introduced, this threshold should be set at such a level that not many M&A transactions – within and in particular outside the EEA – exceed it.

- ***Purchase price is not a suitable and objectively measurable jurisdictional criterion***

Setting the transaction size as a new jurisdictional criterion would constitute a far-reaching fracture in the European merger control system. The purchase price as an essential component of transaction size is not always a reflection of the real market power of a company. The introduction of a jurisdictional threshold based on transaction size would lead to significant practical problems and increase the complexity of the (already complex) jurisdictional thresholds for EU merger control even further.

Determination of the transaction size can be very difficult and is often anything but unambiguous. This is the case, for instance, if the purchase price is paid partially or completely in the acquirer's shares, the value of which changes daily. The same applies for so-called “earn-out” agreements because, in these cases, the initially low purchase price can also still increase as a function of the acquired company's subsequent performance. In innovation-driven sectors, too, there are frequently contractual configurations whereby the value of the transaction is not yet firmly established at the time the contract is concluded. This relates in particular to cases where rights to products which are still in the research or development phase are transferred. Several years can pass before they come to market; the project could also be a complete failure. The consideration in such cases typically comprises a down payment when the agreement is concluded and further partial payments (“milestone payments”) which are dependent on certain conditions being met. This might be reaching a further phase in the development process, grant of the necessary permits or authorisations or reaching certain turnover thresholds once the product comes to market.

It would be very difficult and fraught with uncertainties if companies had to calculate the value of possible milestone payments when the initial contract is concluded in order to verify whether a notification obligation is necessary for merger control purposes.

These difficulties and uncertainties surrounding determination of the transaction size run counter to the need for objectively measurable jurisdictional thresholds, one of the central principles of the ICN Recommended Practices. Objectively measurable jurisdictional thresholds are of decisive importance for the parties to a transaction in order to ascertain whether or not there is a notification obligation in a particular jurisdiction. Since this test is a responsibility of the parties to a transaction, objective measurability is all the more important since a wrong decision by the parties can entail considerable negative consequences. There is otherwise the risk that companies will notify transactions purely by way of precaution in order to be on the safe side. Equally, objectively measurable jurisdictional thresholds serve the interests of the Commission because it can be clearly determined when a transaction is subject to merger control and accordingly case-specific questions, consultations and disputes can be avoided.

In any event, an estimation of the purchase price by the Commission must be ruled out – companies could otherwise no longer determine for themselves with legal certainty whether or not a transaction is subject to merger control.

Another element arguing against the introduction of a jurisdictional threshold based on transaction size is the fact that the US system, which has such a jurisdictional threshold, is an exception among merger control regimes worldwide and that far-reaching rules have been developed to create greater objectivity for the threshold based on transaction size. Nevertheless, these rules are often also very complicated and unclear in application.

Thus, insofar as the Commission wishes to establish the transaction size as a new jurisdictional criterion despite the criticisms set out above, a legally certain definition would have to be found in order to remove uncertainties not only for the parties to the transaction but also for the European Commission. It is particularly important to clarify that the transaction size can be taken into consideration only to the extent that it can be clearly determined at the time when the agreement is concluded (cut-off date) so that no legal uncertainty can arise, for example in cases where there is an “earn-out” clause. Future prognoses should be systematically excluded from consideration with regard to determining the notification obligation.

C. Referral system

The Commission has once more taken up its reflections on amendments to the referral system set out in the 2014 white paper “Towards more effective EU merger control” where it proposed first a facilitation of referrals to the Commission in the pre-notification phase in accordance with article 4 paragraph 5 EUMR and second following notification in accordance with article 22 EUMR. BDI already spoke out in favour of the plan to facilitate and streamline the referral system in its responses to the consultations in 2013 and 2014. A reduction in the

necessary steps is the right route insofar as this can genuinely bring about a simplification and streamlining of procedures.

- ***Referrals in the pre-notification phase in accordance with article 4 paragraph 5 EUMR***

The Commission wants to reduce the number of steps necessary for referrals of cases by the Member States to the Commission. BDI is in favour of a direct notification to the Commission if a planned merger would normally have to be investigated by three or more national competition authorities.

Companies often have a great need to rule out multiple notifications and therefore for their mergers to move into the exclusive competence of the European Commission. For companies which have to notify cross-border mergers in different Member States, multiple national notifications mean an increased administrative effort and high additional costs internally and externally. The problem of multiple notifications has become even more serious in the enlarged Union. Multiple notifications can be assessed as an indicator for the cross-border consequences of a merger initiative which justifies such mergers being dealt with at European level.

The fact that the Member States have so far made hardly any use of their veto right shows that the European Commission's competence for these cases is not seriously in doubt. While the extremely small number of vetoes is a positive signal, this nevertheless does not remedy the weaknesses of the referral rules since the Member States have complete discretion to oppose referral of a case with a European dimension which does not meet the turnover criteria.

Notification of a merger project direct to the European Commission which could then immediately start the case examination would be regarded as great progress for reasons of procedural streamlining and time-saving, since a subsequent referral to the European Commission would be activated in most cases. Such an approach would come very close to the 3-Plus system originally proposed by the European Commission and which BDI has explicitly endorsed in the past.

To take account of the circumstance that the European Commission addresses the content from the outset, it could be considered whether the Member States' veto right should be scrapped and replaced by a procedure whereby the Member States which are against the referral send a substantiated position to the Commission. The final decision would lie with the Commission. Such a scrapping of the veto right would be desirable, since the company in question would have to repeat the notification and submit it to the relevant national competition authorities in the case where a Member State files an ex-post veto against the referral to the Commission – leading to a considerable loss of time and resources.

Alternatively, if the veto right is maintained, it could be considered whether national competition authorities should be allowed to require a referral only if there are weighty reasons, for instance if legitimate national interests are at stake. This seems to be a good idea to avoid duplicate work by several antitrust authorities. Inasmuch, it would also be helpful if the examination period within which the Member States can lodge a veto were to be shortened from fifteen to ten days.

In addition, a further useful improvement to the current system could be achieved if the Commission could restrict the geographical reach of its investigation to the Member States which would have been competent for examination of the transaction. The unnecessary collection of information from unaffected jurisdictions could be avoided in this way.

- ***Referrals to a Member State in the pre-notification phase in accordance with article 4 paragraph 4 EUMR***

Similar possibilities to streamline and accelerate the procedure also exist in the case of referrals in the pre-notification phase by the European Commission to the Member States (article 4 article 4 EUMR). Thought should be given to shortening the referral periods in these cases too. It can be envisaged that the European Commission decides on the referral application within fifteen working days and the Member State gives its consent within ten days. BDI welcomes the proposed scrapping of the proof from the parties to the merger that a takeover would considerably distort competition in a market.

- ***Referrals to the Commission following notification, article 22 EUMR***

The Commission has also proposed in its white paper that only the national competition authorities competent for the investigation of a merger should be able to lodge a referral application with the Commission within fifteen days of notification or announcement of a merger. If the Commission accepts the referral, it could take into consideration not only the territory of the Member States applying for a referral but the entire EEA when it investigates the merger. The consent of the Member States for the referral application should be replaced by a veto right of the other competent national competition authorities.

BDI supports the Commission's proposal. In this way, article 22 EUMR could become a further efficient instrument to deter multiple notifications. The Member State's consent should be replaced by a veto right, for practical reasons. The European Commission should then also have the exclusive competence to assess the case EU-wide, to prevent contradictory decisions and ensure legal certainty for companies. In such cases, it would be desirable if the Commission could restrict the geographical range of its investigation to the Member States in which the transaction would have been subject to notification in order to prevent the unnecessary collection of information from unaffected jurisdictions and the associated considerable effort for the companies involved.

Lastly, article 22 EUMR can become particularly useful if a case can also be referred to the European Commission when the Member States reach different decisions in the substantive examination.

Currently, in one merger case multiple referrals could occur. Hence, for reasons of legal certainty and streamlined procedures (time and cost savings), BDI reiterates its call for referrals nevertheless only to be possible at a single point of time instead of in a series of staggered referral procedures in accordance with article 4 paragraphs 4 and 5 EUMR on the one hand and articles 9 and 22 EUMR on the other hand. Alternatively, referrals in accordance with articles 9

and 22 EUMR should be ruled out after referrals have been made in accordance with article 4 paragraphs 4 and 5 EUMR.

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D. Technical aspects

Further simplifications to EUMR by changing technical aspects are possible. In particular, the allocation of turnover of jointly controlled joint ventures should be changed. It is extremely difficult for the companies involved to make the corresponding figures available, since the latter do not form part of the accounts of the consolidated companies. In the case of asset managers, it is often not clear which revenue streams should be counted as part of the relevant turnover. The Commission should supplement its consolidated jurisdictional notice.