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M E M O R A N D U M

Reform of EC Merger Control

The European Commission issued a "Green Paper" concerning potential changes to the EC merger control regime. The Green Paper solicits comments from third parties, including members of industry, on matters of significant importance to the future of EC merger control. Among the issues being explored is the possible reform of the main jurisdictional and substantive tests under the EC Merger Regulation. The following is a brief summary of the main topics up for discussion:

1. The Jurisdictional Test of the EC Merger Regulation

a. The Existing System

The aim of the Merger Regulation's jurisdictional test is to give the Commission exclusive competence to review mergers and other forms of concentration that are of a Community interest, and to the extent possible, to avoid the need for companies to make multiple merger control filings to national authorities within the EU. As currently drafted, the Merger Regulation has two alternative turnover-based threshold tests. The Commission has exclusive jurisdiction within the EU to review all concentrations where the merging parties meet the thresholds in at least one of these two tests. In this sense, the Merger Regulation provides a "one-stop shop" for all concentrations meeting the thresholds.

b. The Potential Reform

Although the alternative tests are designed to reduce the occurrence of multiple filings within the EU, there are still a large number of concentrations each year that do not meet these thresholds and are subsequently notified in multiple Member States. In 2000, nearly 10 times more notifications were made to Member State authorities than to the Commission. The Commission notes that the number of concentrations that are notified in three or more Member States is increasing, and this practice is expected to become even more frequent as the EU enlarges to include more Member States.

After conducting a detailed study in which the Commission considered a number of options to solve this perceived problem, including a lowering of the various thresholds, the Commission's proposal in the Green Paper is to amend the second alternative threshold test. The amendment would provide that any concentration that would otherwise need to be notified in three or more Member States would automatically fall within the Commission's exclusive jurisdiction. As a result, no concentration would be reviewed by more than two merger control authorities within the EU.

c. Significance

As the purpose of the jurisdictional test in the Merger Regulation is to give exclusive jurisdiction to the Commission to review concentrations with a "Community dimension", it stands to reason that concentrations that would otherwise need to be notified in three or more Member States, and are therefore particularly likely to involve cross-border interests, should be handled exclusively by the Commission.

The Commission's proposal has two main benefits to merging companies. First, by ensuring that no more than two notifications in the whole of the EU will be required for any merger, the costs to companies of multiple filings and the ensuing administrative burden and drain on company resources would be reduced. Second, by limiting the number of authorities with jurisdiction to review a merger, there would be a smaller risk of the entire merger being thwarted by the prohibition decision of a single authority.

At the same time, the general perception is that the Commission is in some respects better equipped to handle complex cases, and more stringent in its analysis, than some Member State authorities. As a result, the Commission may be more likely than its national counterparts to identify and analyse some potential competition issues (for example concerning vertical effects of concentrations and cooperative aspects of joint ventures). For this and other reasons, there may occasionally be cases where, despite the additional cost and burden, it would be considered more desirable to notify a concentration to three or more Member States than to the Commission, assuming the EC thresholds are not met. The Commission's suggested amendment to the jurisdictional test would eliminate this possibility.

It should also be mentioned that it is not clear how this amendment would work in practice. Currently, Member States have considerably different tests for determining jurisdiction. Some Member States employ turnover-based threshold tests, which vary from Member State to Member State, while others use a combination of turnover and market share thresholds. Moreover, although nearly all the Member States have or will soon have mandatory filing requirements for mergers, provided the thresholds are met, the United Kingdom and Luxembourg still have voluntary systems, which means that turnover achieved in these Member States would not be as important as turnover achieved in Member States with mandatory filing rules for the purposes of determining whether the Commission has jurisdiction. In addition, the definition of a notifiable concentration and the method for calculation of turnover differs between Member States.

The above factors could make it more difficult and time consuming for companies to determine whether a transaction must be notified to the Commission or to national authorities. Recognising this, the Commission has suggested that the requirement that an EC notification must be made within one week of the conclusion of a binding agreement (among other things), might need to be amended or repealed. The idea of harmonising the jurisdictional rules of the Member States, which had been mentioned by the Commission in recent months and would greatly facilitate the assessment of whether the thresholds are met in three or more Member States, is not discussed in the Green Paper.

2. The Substantive Test of the EC Merger Regulation

a. The Existing System

Under the present system, if a transaction falls within the scope of the Merger Regulation, the Commission will examine whether it creates or strengthens a dominant position of the parties involved on the relevant market with the effect of significantly impeding effective competition in the EU or in a substantial part thereof. If it does, it will be prohibited, unless the parties can offer commitments that would eliminate these problems. The Commission tends to view the concept of "dominance" as the ability to act independently of market forces. In particular, the Commission will usually consider a company that is able to increase prices without losing business to competitors as having a dominant position.

b. The Potential Reform

While the Commission's substantive test focuses on "dominance", other major jurisdictions, such as the United States, Canada and Australia, use a "substantial lessening of competition" test to assess the legality of concentrations. While the difference in substantive approaches does not fully explain recent divergences in conclusions between the Commission and US authorities, such as in the GE/Honeywell case, it has been argued that a global convergence in approaches would be facilitated by having a uniform substantive test among the major merger control authorities. The Commission also admits that a "substantial lessening of competition test" may be more

appropriate than a dominance test in dealing with certain anti-competitive aspects of mergers.

Complicating matters, however, is the fact that many EU Member States now have adopted a dominance test in order to be consistent with the Commission's approach. The Commission recognises that a change in the EC substantive test could have the effect of creating greater alignment of merger control rules internationally while leading to greater disparity within the EU. The Commission therefore invites comments on whether the dominance test should be replaced with a significant lessening of competition test, but at least for the moment, the Commission is reserving its judgement on this issue.

c. Significance

It is generally considered that the "substantial lessening of competition" test is less rigid than the dominance test, in that it allows objections to be raised against mergers which, although not creating or strengthening a dominant position, may nevertheless reduce competition. It has been claimed that the requirement of finding dominance may have a straightjacket effect on the ability of the Commission effectively to protect competition.

However, if there is a gap in the EU merger control regime resulting from the dominance test, it is not apparent that many mergers fall through the cracks. Instead, the Commission has thus far been successful in moulding the dominance test in order to apply it to an array of perceived competition problems arising from mergers. For example, what the Commission refers to as the creation or strengthening of a "collective" dominant position might more appropriately be categorised as a substantial lessening of competition. Hence, arguably the main effect of changing the substantive test is that it would require less manoeuvring on the part of the Commission to justify its objections to mergers, perhaps leading to greater transparency and consistency in Commission decisions.

Although it is debatable how far in practice the EU is from applying a "substantial lessening of competition" test, one possible benefit of officially adopting such a test is that this would put added pressure on the

Commission and on US antitrust authorities to reach common conclusions on the legality of mergers being reviewed on both sides of the Atlantic, especially where world-wide markets are concerned. Divergent conclusions by EU and US authorities concerning the same merger would be harder to defend if both authorities were using an identical substantive test.

An additional potential advantage to companies of the adoption of a "substantial lessening of competition" test is that it might lead the Commission to moderate its views on efficiencies generated by mergers. It is often surprising to those with experience of the US merger control system that such efficiencies can be regarded as a negative factor in the competition analysis under the Merger Regulation (in contrast, in the US, efficiencies are a recognised defence in a merger review). In the EU, where dominance is the key consideration, efficiencies have traditionally been analysed in terms of the competitive advantage conferred on the merged firm, and thus considered as a factor creating or strengthening a dominant position. A "substantial lessening of competition" test might enable the Commission to see efficiencies in a more positive light and in a manner more consistent with prevailing economic theory.

3. Other Issues Open for Discussion

The Commission is also considering and welcomes comments on various other issues concerning possible reform, including the following:

- Whether the rules on the timing for submission by parties of commitments needed to settle cases should be amended, in particular to allow the parties to agree to "stop the clock", i.e. to suspend the statutory review period in order to allow the Commission more time to assess and market test submitted commitments.

- Whether the concept of a "concentration" (i.e. a transaction that is notifiable under the Merger Regulation) should be expanded to include certain acquisitions of non-controlling minority shareholdings, strategic alliances of definite duration, "partial-function" production joint ventures or venture capital transactions.

- Whether there should be an amendment to the Merger Regulation that would lower the criteria a Member State must meet in order for the Commission to refer the review of a concentration that is normally within the Commission's exclusive jurisdiction to that Member State, and that would allow the Commission to refer certain cases to the national authorities on its own initiative.

- Whether the Commission's powers of investigation and enforcement in merger cases should be increased, for example, by allowing the Commission to take oral statements as evidence, and by replacing lump sum fines for infractions such as failure to notify with fines based on percentage of the company's turnover.

- Whether the recently introduced "simplified notification procedure" for harmless mergers should be replaced by a block exemption regulation that would eliminate altogether the need to notify such transactions.

- Whether the Commission should require that notifying parties pay a filing fee, and if so, whether this should be a flat fee or a fee based on the complexity of the notified transaction.

- Whether the calculation of time limits under the Merger Regulation should be made more transparent, for example, by reference to the number of working days for each stage of the proceeding.

- Whether the Commission should be given a legal deadline after which it cannot declare a submitted notification to be incomplete.