

MLex Ab Extra:

The Urge to Merge

Anne MacGregor of Baker & McKenzie sheds light on the difficulties facing companies in getting mergers through the antitrust process in Europe



Anne MacGregor

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THE URGE TO MERGE

Anne MacGregor examines the issue of EC Merger Regulation reform

The current EC Merger Regulation has been operational since May 2004.¹ On 21 September 2010, EU merger control will celebrate its twentieth anniversary.² As the EU's newly appointed Commissioner for Competition Joaquín Almunia takes the reins in Brussels, many in the European antitrust community are hoping that the changing of the guard will bring with it a genuine willingness to reform various aspects of merger control.

Some Brussels bureaucrats like to fall back on the old adage “if it's not broken, then don't fix it.” It would be impossible to make the case that the Merger Regulation is “broken” to the extent that it no longer runs at all. But like all complicated machinery, it needs regular servicing to keep it humming along at optimal performance levels. The European Commission has a constitutional role as the initiator of legislation, and as such, it falls to DG Competition, the keeper of this particular piece of machinery, to engage in some thoughtful maintenance, in consultation with users, so that it can in due course put before the Council its considered recommendations for improvement.³

The time is surely ripe. In late 2008 and early 2009 DG Competition consulted with Merger Regulation stakeholders on the functioning of the Regulation's jurisdictional provisions as part of its obligations to report to the Council by 1 July 2009 on the operation of the turnover thresholds and referral mechanisms.⁴ The Commission's resulting Communication and Staff Working Paper on these aspects,⁵ presented by Commissioner Kroes on 18 June 2009,⁶ are useful and informative documents. But many outside the Commission who had participated in that review process were left disappointed.⁷ The exercise had to be done when it was done because there was a requirement to report to the Council in the Merger Regulation itself by the 1 July 2009 deadline.⁸ But there was no political appetite in the waning months of Commissioner Kroes' reign to grasp any of the learning or ideas that were aired during that process and translate them into real reforms. This article will touch upon just a few of those ideas.

On the jurisdictional front, too many companies are having to waste time and money notifying the establishment of foreign joint ventures which will have absolutely no activities or

impact within the EU. The irony is that when such JVs have multinational groups as parents, the transaction often satisfies the EU-wide turnover thresholds and is also “full function.”⁹ It is of little comfort for business that “only a Short Form” notification is required in these circumstances.¹⁰ Common sense dictates that an amendment to the Merger Regulation is necessary so that the Commission does not keep having to invest its own scarce resources examining the establishment of all these so-called “canteens in Tanzania.”¹¹

Another issue which needs to be examined is the lack of flexibility in the phase I timetable under the Merger Regulation. Under Commissioner Kroes, probably more so than under previous Commissioners, a number of cases went into phase II in which Statements of Objections were never issued.¹² The “serious doubts” that the case team had at the end of phase I were able to be resolved with just a bit more time. These cases show what every merger control practitioner knows: sometimes 25 or even 35 working days is not long enough for a phase I.

Sometimes that is because the procedure can be manipulated by third parties who want to throw a spanner in the works. A well-advised complainant knows that he can bide his time to his own advantage during pre-notification and in the first few weeks of phase I. Then, around the time when market investigation questionnaires are due back on the case team's desk, the submission of a serious-looking submission, invariably including impressive economic analysis, putting forward a not implausible theory of harm, sets the proverbial cat among the pigeons. The case team and the Chief Economist's Office will not have time then to properly consider the new submission before the phase I deadline. And the notifying party cannot be given an adequate opportunity to counter the matters that the third party has raised. The seeds of doubt having been firmly planted in the regulator's mind, there is little option but to put the case into phase II. Impala's successful challenge to the Sony BMG tie-up means that every case handler knows the clearance decisions they write must be adequately underpinned and “challenge proof.”¹³

Third parties must be able to have their say, and one can understand the administrator's dilemma. But the practical

impact of putting a case into phase II for the parties to the transaction can be monumental, regardless of the ultimate outcome weeks or months later. There is a sense among the antitrust community that often DG Competition officials, many of whom have never worked in the private sector, have little grasp of the fall-out an Article 6(1)(c) decision can unleash. A phase II means that it is suddenly unclear when (or if) the transaction will close. Share prices can dive, sometimes quite dramatically. The delay very often equates with a substantial devaluing of the business being acquired. Management and employees in that business face extreme uncertainty. In late 2009, the risk of further layoffs at Sun Microsystems in light of its already precarious financial position prompted a group of US senators to write to the EC urging it to clear Oracle's acquisition of Sun as soon as possible.¹⁴

There are solutions. The most simple would be to build in a mechanism for the notifying party to be able to unilaterally prolong phase I. The existing "stop the clock" mechanism can and has been used on occasion to buy time in phase I (as have very late declarations of incompleteness), but "stop the clocks" are rather more often and certainly more appropriately used in phase II.¹⁵ In any event, a formal suspension currently relies on the Commission to find (at least on paper) that a party has not responded to an information request by a given deadline. It is true that "stop the clocks" are at times "manufactured" to the benefit and with the blessing of the notifying party. But there is a case to argue that because going into phase II can be so devastating for companies, the notifying party should have a unilateral right to be able to buy itself time, within reasonable limits.

On the broader theme of sensitising DG Competition officials to the insecurities and other realities of the private sector, there are also solutions, which do not require legislative reform. In Washington, professionals move constantly between law firms, economic consultancies and other private-sector organisations and the administration as a matter of course, particularly when an administration changes. In the US, this practice is widely perceived to be utterly healthy.

No one would assert that DG Competition's officials are not highly educated and intelligent people. For the most part, the open competition selection process ensures that they have the necessary academic qualifications and requisite language skills when they go in to the Commission, usually at the beginning of their careers. But some things can only be truly understood as a result of exposure to life outside the hallowed and protected corridors of a civil service. For example, a lawyer who has had to work through the night in private practice to compile a questionnaire response, who later finds himself composing information requests inside DG Competition as a case handler

will comprehend the real-life practicalities of extracting detailed and precise information out of global businesses in very short time frames. It is to be hoped that as a result of his experiences in the private sector, he would be able to formulate such requests within reasonable parameters and in consultation with the companies concerned to understand what information is available.

DG Competition's staffing policy needs to incorporate a "revolving door." In the same way that lawyers are often seconded in-house to their clients, DG Competition officials would do well to spend time inside law firms, consultancies and businesses. Everyone would benefit.

Increased real-world exposure by DG Competition officials may also go a long way to addressing the naivety which can have a tendency to entrench itself in some case teams. Often a simple truth seems to get lost: case teams are not prosecutors. The case team's job is to assess whether the substantive test for clearance under the Merger Regulation is met.¹⁶ It has to look for that truth. In today's world, sophisticated economic techniques can very often reveal that truth, or put another way, disprove a particular theory of harm. Phase II decisions such as that in Ryanair/Aer Lingus, which include many pages of economic analysis, demonstrate that the "truth" in merger cases these days is invariably empirical and data-based.¹⁷ Words alone won't cut it.

DG Competition has its own team of in-house economists. But some would argue that the integrity and independence of the Chief Economist's Office is not as it should be. Members of the Chief Economist's Office who sit on case teams comprised

of non-economists should be there to assert and explain the value of their discipline. If a case team wants to start pursuing a particular theory of harm, the economist on the case team should be able to explain how the Chief Economist's Office can help to test that theory and assist in the evaluation of external economic analysis presented by business. That may in the end involve standing behind external economic work which has been internally tested and found to be robust, and as such, standing up to the non-economists on the case team.

It may also be appropriate during a case for external economists to meet with members of the Chief Economist's Office without the usual bevy of non-economist hangers-on from either side, for example, to discuss the appropriateness of particular data sets. Such meetings used to be common practice: these days they have all but disappeared. In the US antitrust system, the economists' divisions are separate: two separate reports are put before decision-makers – one from the case team and one from the economists. One suggestion for reform would be for

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the Chief Economist's Report to be published in its own right after the final decision. Then it would be open to peer review. There is presently no internal or external scrutiny of the work done by Commission economists on merger cases. The courts in Luxembourg are never going to be equipped or minded to delve into those details.

European big business is not inherently anti-competitive, and notifying parties do not set out to hoodwink the regulator when they notify their deals. Without credible economic evidence that supports a substantive theory of harm, a case team should not push for formal remedies "just because it can." TomTom/TeleAtlas and Oracle/Sun Microsystems are both recent phase II examples in which the parties resisted pressure to submit formal remedies.¹⁸ Their gamble paid off in terms of achieving unconditional clearance: the regulator did not have the appeal-proof evidence to prohibit those transactions at the end of the day, but the companies paid a high price in business terms because they had to endure every last minute of a phase II procedure.

Although they only occur in a few of all phase II cases,¹⁹ late in

the procedure, when done right, an oral hearing can provide the parties with a fresh opportunity to present their case to people in the DG Competition hierarchy who are not part of the case team. In late 2009, Oracle was extremely outspoken during the hearing concerning its acquisition of Sun Microsystems, arguably a turning point in the case. Lucky for it, on that occasion, relevant individuals in the decision-making hierarchy were in attendance.

The Merger Regulation's "user community," i.e. antitrust law practitioners, competition economists, public affairs consultants, and above all, the companies for whom they act, are widely of the view that the Merger Regulation and the administrative practices surrounding the legislation should be revisited under Commissioner Almunia. A good deal of useful work has already been done which can contribute to this process. Now we have to hope that the political willingness to drive real outcomes will be there. ■

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Footnotes

- 1 Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings (the EC Merger Regulation), OJ L 24/1, 29.1.2004.
- 2 Council Regulation (EEC) No 4064/89 entered into force on 21.9.1990.
- 3 Council adoption is only required for amendments to the EC Merger Regulation itself. The so-called Implementing Regulation, which includes model notification forms and other procedural requirements, is a Commission Regulation.
- 4 The Commission's consultation document can be viewed at http://ec.europa.eu/competition/consultations/2008_merger_regulation/index.html
- 5 COM(2009)281 final, 18.6.2009, Communication from the Commission to the Council, Report on the Functioning of Regulation 139/2004, available at http://ec.europa.eu/competition/mergers/studies_reports/report_139_2004_en.pdf and SEC(2009)808 final/2, 30.6.2009, Staff Working Paper accompanying the Communication, available at http://ec.europa.eu/competition/mergers/studies_reports/staff_working_paper_report_139_2004_de.pdf
- 6 Press Release IP/09/963 of 18.6.2009 "Merger Regulation contributes to more efficient merger control in EU."
- 7 Contributions received in response to the consultation are available at http://ec.europa.eu/competition/consultations/2008_merger_regulation/contributions.html
- 8 Articles 1(4) and 4(6) of the EC Merger Regulation.
- 9 Articles 1(2) and 5 of the EC Merger Regulation.
- 10 See the model Short Form, paragraph 1.1.1, Annex II to Commission Regulation (EC) No 802/2004 of 21 April 2004 implementing the EC Merger Regulation, OJ L 133, 30.4.2004, p. 31.
- 11 Some academic literature argues that in such circumstances, the Commission cannot have jurisdiction, because in 1999 the then European Court of First Instance held in the Gencor case that the Commission has jurisdiction to review a transaction that is going to result in a direct, foreseeable and substantial effect within the EU. The enforcement risk for companies who choose not to notify in these circumstances would appear to be low.
- 12 See for example Cases M.5440 Lufthansa/Austrian Airlines; M.5141 KLM/Martinair; M.4980 ABF/GBI Business; M.4942 Nokia/Navteq; M.4874 Itema/BarcoVision; M.4781 Norddeutsche Affinerie/Cumerio; M.4747 IBM/Telelogic; M.4734 Ineos/Kerling; M.4731 Google/DoubleClick; M.4662 Syniverse/BSG; M.4647 AEE/Lentjes; M.4523 Travelport/Worldspan; M.4403 Thales/Finmeccanica/AAS & Telespazio; M.4215 Glatfelter/Crompton Assets; M.3975 Cargill/Degussa Food Industry; M.3848 Sea-Invest/EMO EKOM; M.3625 Blackstone/Acetex; M.3178 Bertelsmann/Springer; M.3333 Sony/BMG (2nd notification). Non-exhaustive list.
- 13 Judgment of the Court of First Instance in Case T-464/04, 13.7.2006, Independent Music Publishers and Labels Association (Impala) v Commission of the European Communities.
- 14 Letter of 24.11.2009 by 59 US Senators, led by Senators Kerry and Hatch, available in full at <http://kerry.senate.gov/cfm/record.cfm?id=320244>
- 15 For an in-depth analysis of suspensions and declarations of incompleteness in merger decisions, see further MacGregor, "Merger Regulation Delays," *Competition Law Insight*, 7.4.2009, p. 3 and 5.5.2009, p. 3.
- 16 Article 2(2) of the EC Merger Regulation. The concentration must not significantly impede effective competition in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position.
- 17 Case M.4439 Ryanair/Aer Lingus, Article 8(3) prohibition decision of 27.6.2007, available in full at: http://ec.europa.eu/competition/mergers/cases/decisions/m4439_20070627_20610_en.pdf
- 18 Cases M.5529 Oracle/Sun Microsystems, Article 8(1) clearance decision of 21.1.2010 and M.4854 TomTom/Tele Atlas, Article 8(1) clearance decision of 14.5.2008.
- 19 Hearings took place for example in cases M.3796 Omya/Huber; M.3333 Sony/BMG (2004 notification).