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Sixth Edition

Editor
Simon Robinson

Law Business Research

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EDITOR'S PREFACE

Deal-making has remained on the agenda in the past year, although the first half of 2011 showed a stronger performance than the second half, which saw a significant fall in transactional activity. In the wake of continuing economic uncertainty, opportunities for acquisitions remain limited to companies and institutions on a stable financial footing. At the same time, corporates are beginning to focus on their core business and looking for ways to return value. Valuations remain favourably low for purchasers, and the prospect of striking a bargain makes cross-border M&A attractive for those who can afford it. While access to the loan market has remained difficult, cash-rich corporations have begun to swing the balance in their favour. Shareholder participation and a desire for control and accountability are on the rise, and an atmosphere of increased regulation, reform and austerity is building. We remain in a state of geopolitical flux, and these factors continue to complicate the global economic scenario. The period of widespread unrest in the Middle East and North Africa seems to be reaching a settled conclusion, although the situation in Syria (and possibly Mali and Sudan) is still volatile. A number of countries have seen fresh elections and a transition of leadership, including France and Russia, and a change of leadership in China is expected following the 18th National People's Congress this autumn, when the US presidential elections will also take place. The sovereign debt crisis and the ongoing uncertainty over the fate of the eurozone are further contributing to the lack of confidence in the markets.

All is not doom and gloom, however, and whereas the global picture remains difficult, there are signs of hope. The emerging markets have shown a persistent growth in outbound investment, spurred on by a desire to build a more prominent global presence and for the purpose of accessing new markets. European targets remain of interest to both US and Middle and Far-Eastern buyers. Inbound investment from the emerging markets into both Africa and Australia is on the rise, and this has strengthened activity in the energy, mining and utilities sector. The technology, media and telecoms sector has also shown signs of promise with some high-profile deals, and must be watched with interest in the coming year. There is hope that, as political and economic factors

stabilise, M&A activity will once more gather pace and momentum, and enter a new era of resurgence. We shall see.

Once again, I would like to thank the contributors for their continued support in producing this book. As you read the following chapters, one hopes the spectre of the years past will provide a basis for understanding, and the prospect of years to come will bring hope and optimism.

Simon Robinson
Slaughter and May
London
August 2012

Chapter 2

EUROPEAN COMPETITION

Götz Drauz and Michael Rosenthal[1]

During the past 12 months, the EU's merger control regime again produced headlines in the business news reminding deal makers how important it is to get it right with the European Commission.

Not all of the stories about Brussels had a happy ending. For example, despite significant pressure and intense lobbying, the Commission blocked the stock exchange merger between Deutsche Börse and NYSE Euronext.

This chapter will address this case and other notable developments that took place between 1 July 2011 and 30 June 2012[2] following a brief summary of the most important rules that practitioners need to understand when faced with the possibility of an EU merger control filing.

I JURISDICTION

i Overview

The Commission has exclusive jurisdiction to review 'concentrations with a Community dimension'. Pursuant to Article 3(1) of the EU Merger Regulation,[3] a 'concentration' is deemed to arise 'where a change of control on a lasting basis'[4] results from either the merger of two or more previously independent undertakings, or the acquisition of

1 Götz Drauz and Michael Rosenthal are partners at Wilson Sonsini Goodrich & Rosati, LLP.

2 Overall, the number of mergers notified to the European Commission in 2011 evidence that merger activity has not nearly reached pre-downturn levels. 309 mergers were notified in 2011, less than in 2008 (347) but still well above the number in 2009–2010 when the number of filings ranged from 259 to 274.

3 Council Regulation (EC) No. 139/2004 on the control of concentrations between undertakings.

4 The use of warehousing schemes, whereby assets are held temporarily by a financial institution pending their transfer to the ultimate purchaser, may not require notification in certain strictly

control (direct or indirect) of the whole or part of one or more undertakings by one or more other undertakings.

The 'Community dimension' test is turnover-based, and takes into account both the worldwide and EU turnover of the undertakings concerned by the transaction.[5] Concentrations that do not have a Community dimension may be reviewed by the competition authorities of the Member States applying national law. This 'bright-line' allocation mechanism is complemented by the possibility for cases to be reallocated from the Commission to the Member States and *vice versa*, under a system of referrals.

The case reallocation scheme provides that a referral may be triggered after a notification and, since the new Merger Regulation took effect in 2004, also before a filing is made: (1) Article 4(4) and (5) of the EU Merger Regulation provide for the possibility of pre-notification referrals at the initiative of the notifying parties;[6] while (2) Articles 9 and 22 of the EU Merger Regulation provide for the (more burdensome) possibility of post-notification referrals triggered by one or more Member States.

ii Recent developments

The downsides of the EU's post-notification referral system were recently highlighted in *Liberty Global/KBW* where the Commission's decision to refer the review of Liberty Global's acquisition of KBW to the German Bundeskartellamt under Article 9 of the EU Merger Regulation created significant delays, resulting in a total duration of approximately eight months from the date of notification to the Commission until the Bundeskartellamt's clearance decision.

While the delay may have been primarily due to the substantive concerns raised by the merger and extensive remedies discussions, an estimated one and half month at least (not including the usually time-consuming pre-notification discussions with the Commission) is attributable to the time needed for the Commission to consider Germany's referral request and that needed for the Bundeskartellamt to accept the parties' notification following the Commission's decision to grant the referral.

Therefore, in cases with well-known national sensitivities resulting in a rather high referral risk, merging parties are well advised to address jurisdictional questions with the Commission and the national competition authorities concerned at an early (ideally pre-notification) stage. Ignoring a referral risk and filing directly with the Commission without any consultation with the respective national competition authority is unlikely

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defined circumstances. See Case T-279/04 (*Editions Odile Jacob v. Commission*), judgment of 13 September 2010.

5 Article 1(2) and (3) of the EU Merger Regulation.

6 Of particular importance in this regard is the '3-plus rule' set out in Article 4(5) of the EU Merger Regulation, pursuant to which the notifying parties in a concentration that does not have a Community dimension may nevertheless apply to have the Commission review the transaction, in order to avoid having to file in multiple jurisdictions within the EU, provided that the transaction is notifiable under the laws of at least three Member States, and no Member State objects to the referral.

to be met with much sympathy by the latter, which, in case of a referral, will have the last word on the deal's destiny.

In this context, reference is made to the recently issued 'Best Practices on Cooperation between EU National Competition Authorities in Merger Review' (November 2011),[7] which encourage the merging parties to contact each of the NCAs concerned as soon as practicable and provide them with the required information to assess any jurisdictional questions. The Best Practices thus aim at 'facilitating the smooth functioning of the reattribution mechanisms'.

Similarly, the Commission and the US Antitrust Authorities jointly issued revised Best Practices on Cooperation in Merger Investigations[8] that provide guidance for merging parties to facilitate coordination between the authorities. While coordination between agencies is likely to be beneficial for the merging parties in some cases, there are circumstances where it may be in the interest of the parties to the merger to seek early clearance in one jurisdiction rather than seeking a coordinated outcome.[9]

II PROCEDURE

i Overview

When the jurisdictional test is met, notification to the Commission is mandatory and must be made prior to implementation. The notification itself can be made at any time once a recognised 'triggering event' has occurred. There is no filing deadline. The formal notification of a concentration to the Commission is usually preceded by confidential contacts with Directorate-General of Competition, in which the proposed transaction and the filing requirements are discussed, frequently in great detail.[10]

Once notified, the vast majority of cases is cleared by the Commission (sometimes subject to remedies) after what is called a Phase I inquiry (lasting 25 to 35 working days); harder cases are subject to an in-depth Phase II review (lasting a further 90 to 105 working days). The Merger Regulation makes provision for further extensions of up to 20 working days in Phase II, at the request or with the consent of the parties, and such extensions are now common.

Notifying parties must not implement a notifiable concentration before having received clearance. Violation of the suspension obligation can lead to the imposition of a fine of up to 10 per cent of the aggregate turnover of the notifying party or parties

7 Available on the European Commission's website at http://ec.europa.eu/competition/ecn/nca_best_practices_merger_review_en.pdf.

8 Available on the European Commission's website at http://ec.europa.eu/competition/mergers/legislation/best_practices_2011_en.pdf.

9 This may be the case, for example, where there are good reasons to believe that early clearance will be granted in one jurisdiction and not in the other.

10 See 'DG Competition Best Practices on the conduct of EC merger control proceedings', 20 January 2004, available at: http://ec.europa.eu/competition/mergers/legislation/proceedings.pdf.

(Article 7 of the EU Merger Regulation). The Commission has a policy of imposing fines in such circumstances.[11]

ii Recent developments

Controversy has arisen where several mergers in the same market have been notified to the Commission at close intervals. In such cases, the Commission takes a 'first-come, first-served' approach, and will review the competitive effects of the first transaction without having regard to a second one, but taking into account the first transaction in the assessment of the second. This can be problematic, in particular when the time difference between the two notifications is insignificant.

These issues were highlighted in two recent cases. On 19 April 2011, a concentration whereby Seagate would acquire Samsung's HDD business was notified to the Commission one day in advance of the notification of the acquisition by Western Digital of Hitachi's HDD business. *Seagate/Samsung* benefited from the priority rule even though the *Western Digital/Hitachi* MoU was signed earlier and the parties had initiated informal discussions with the Commission well before the other side.

Pursuant to the priority rule, the Commission analysed the *Seagate/Samsung* transaction as if the *Western Digital/Hitachi* transaction were not taking place, while the latter deal was reviewed in light of the market consolidation brought about by the former. While *Seagate/Samsung* was cleared without conditions, *Western Digital/Hitachi* had to agree commitments with the Commission in order to gain clearance.[12] Western Digital has lodged an appeal with the General Court in Luxemburg.

The Commission's approach in such cases substantially differs from the approach adopted in other jurisdictions, notably the United States, Japan and Korea, and makes cooperation with such other authorities on transnational deals more complex. One of the lessons of *Western Digital/Hitachi* is that merging parties should engage in confidential pre-notification discussions with the Commission as early as possible in order to be able to proceed with the actual filing on the day of or shortly after the deal's public announcement.

III SUBSTANTIVE ASSESSMENT

i Overview

The substantive test under the EU Merger Regulation is whether the proposed transaction would lead to a 'significant impediment of effective competition, in particular as a result of the creation or strengthening of a dominant position' (the SIEC test). The substantive

11 In 2009, the Commission imposed a fine of €20 million on an undertaking for acquiring *de facto* sole control of a competitor without notifying the operation to the Commission. Case COMP/M.4994 (*Electrabel/Compagnie Nationale du Rhône*).

12 The Commission press releases for both decisions are available on the authority's website at http://europa.eu/rapid/pressReleasesAction.do?reference=IP/11/1213 and at http://europa.eu/rapid/pressReleasesAction.do?reference=IP/11/1395.

assessment of a notified concentration by the Commission thus requires the careful examination of the likely effects of the proposed transaction on every affected market.

This analysis starts by identifying the various types of competitive effects brought about by the concentration (which may co-exist in a single transaction): horizontal effects, arising when the parties to the concentration are actual or potential competitors; vertical effects, arising where the parties are active at different levels of a supply chain; and conglomerate effects, arising when the parties are active on different but related markets.

When the Commission reaches the preliminary conclusion that a concentration raises competition concerns, the parties will be invited to offer commitments (commonly referred to as 'remedies') with a view to securing conditional approval. In fact, being able to structure effective remedies that address the Commission's concerns (without jeopardising the value of the transaction[13]) could make the difference between clearance and prohibition.

The Commission prefers structural remedies to behavioural remedies.[14] More specifically, the Remedies Notice distinguishes 'between divestitures, other structural remedies, such as granting access to key infrastructure or inputs on non-discriminatory terms, and commitments relating to the future behaviour of the merged entity'.[15] Divestitures and the 'removal of links between the parties and competitors' are considered as the 'preferred remedy'.[16]

However, the assessment of the effectiveness of a remedy in a particular case cannot be based on a theoretical framework resulting in a preference for one kind of remedy over another. Instead, an effects-based assessment is required which, on a case-by-case basis, selects the appropriate and proportionate remedy depending on the theory of harm identified by the Commission. Recent cases suggest that the Commission is willing to adopt a more flexible approach, at least in certain industries.[17]

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13 Two prominent examples of withdrawals due to concerns in relation to the scope of the requested remedies are BHP Billiton's attempted acquisition of Rio Tinto (Case COMP/M.4985) and OMV's failed attempt to acquire MOL (Case COMP/M.4799). In March 2011, Merck and Sanofi abandoned their animal health care joint venture before notification, citing 'the extent of the anticipated divestitures' as a major obstacle to closing. Most recently, SC Johnson had to withdraw its notification of the planned acquisition of Sara Lee's household insecticide business (Case COMP/M.5969).

14 See, for example, Remedies Notice, paragraphs 10, 15, 17 and 69.

15 Remedies Notice, paragraph 17.

16 Remedies Notice, paragraphs 58–61 ('Whilst being the preferred remedy, divestitures *or the removal of links with competitors* are not the only remedy possible to eliminate certain competition concerns' [Emphasis added]).

17 The Commission's seemingly less hostile approach to behavioural remedies reflects policy in the United States where the Department of Justice's guide to merger remedies (June 2011) recognises that conduct remedies can preserve a merger's potential efficiencies while remedying competitive harm, and are therefore more flexible than simple structural remedies (i.e., divestitures).

ii Recent developments

Three cases merit a particular mention: the Commission's decision to prohibit the *Deutsche Börse/NYSE Euronext* transaction and the clearance decisions in *Google/Motorola Mobility* and *Microsoft/Skype*.

Deutsche Börse/NYSE Euronext

On 1 February 2012, the Commission issued a highly publicised prohibition decision to block the proposed stock exchange merger between Deutsche Börse and NYSE Euronext, which operate Eurex and Liffe respectively, the two largest exchanges for financial derivatives based on European underlyings.[18]

The Commission found that the merger would have resulted in a significant impediment to effective competition on the market for European financial derivatives traded on exchanges. According to the Commission, the market investigation had revealed that the two companies competed head to head for certain types of products and were each other's closest rivals when it comes to developing new product offerings, and that, due to high barriers to entry, new entrants were unlikely to constitute a credible threat to the merged entity.

In order to remedy the Commission's competition concerns, the parties offered a number of commitments. In particular, the parties offered to divest Liffe's European single stock equity derivatives products and to provide access to the merged entity's clearing for certain categories of new interest rate, bond and equity derivatives contracts; however, the Commission considered these commitments insufficient in scale and scope and unlikely to be verifiable in practice. Deutsche Börse has since appealed the decision before the General Court.

Google/Motorola Mobility

In *Google/Motorola Mobility*, the Commission examined, in particular, whether the acquisition of Motorola Mobility, a supplier of smartphones and tablets, would give Google the ability and the incentive to prevent Motorola's competitors from using its leading Android operating system.[19] Ultimately, the Commission cleared the acquisition because it found it unlikely that Google would restrict the use of Android to Motorola being only a relatively small player in the market.

The Commission's investigation also focused on the acquisition's effects in light of Motorola's significant number of 'standard essential patents' ('SEPs'), i.e., patents that are essential for certain telecommunications standards (e.g., 3G or 4G/LTE) to operate. One specific concern of the Commission was whether Google had the possibility and incentive to use the threat of injunctions against good faith licensees to extract high licence fees and force access to cross-licences.

It is interesting to note in this context that, in addition to its commitment to license SEPs on fair, reasonable and non-discriminatory (FRAND) terms, Google offered a commitment to refrain from seeking injunctive relief under certain circumstances.

18 Case COMP/M. 6166 (*Deutsche Börse/NYSE Euronext*).

19 Case COMP/M.6381 (*Google/Motorola Mobility*).

However, the clearance was not made conditional on theses commitments, as the Commission found that the parties would already be sufficiently constrained by the prospect of an *ex post* investigation under Article 102 of the Treaty on the Functioning of the EU.

Microsoft/Skype

In *Microsoft/Skype*, the European Commission was faced with complex questions of market definition and competitive effects in 'converged' TMT markets where technological divisions that used to help in defining TMT markets are becoming less relevant.[20] The Commission reviewed the transaction's effects on consumer and enterprise communications integrating a wide range of functionalities (instant messaging, voice and video calls) across various platforms (PCs, smart phones and tablets) and operating systems.

As to consumer communication, the Commission concluded that despite an overlap in the parties' activities with respect to video communication, the acquisition did not raise any competition concerns in a growing market that counted numerous players. As regards enterprise communications, the Commission found that Skype did not compete with Microsoft's Lync, a product mainly used by large companies. The Commission also considered conglomerate effects but ultimately cleared the transaction without remedies.

On 15 February 2012, Cisco lodged an appeal before the General Court, mainly arguing that the Commission made a manifest error in assessing the impact of the transaction, in particular in relation to network effects and in view of the high combined market shares in consumer unified communications; it seems questionable, however, whether the court will be prepared to second-guess the Commission's judgment on complex questions of market definition and competitive effects in the fast-moving IT markets.

20 Case COMP/M.6281 (*Microsoft/Skype*).

Appendix 1

ABOUT THE AUTHORS

GÖTZ DRAUZ

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Götz Drauz's practice is focused on EU and German competition law. He has represented companies in some of the most significant merger matters. Named an 'elite' practitioner by *Global Competition Review*, Mr Drauz is recognised in all the principal directories as a leading competition lawyer. Prior to entering private practice, Mr Drauz served at the European Commission for 25 years, most recently as the Deputy Director-General for Competition and previously as the head of the Merger Task Force.

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Michael Rosenthal is the managing partner of Wilson Sonsini Goodrich & Rosati's recently opened Brussels office. He advises clients in a wide range of industries on all aspects of EU and German competition law before the European Commission as well as the national competition authority and courts in Germany. Dr Rosenthal is listed as a leading competition lawyer in all of the major legal directories and is the co-author of *Rosenthal/Thomas, European Merger Control* (C.H. Beck/Hart Publishing, 2010).

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