WILMERHALE

Up Next, More "Killer Acquisition" Reviews at the EU?

New policy to catch transactions that may create competition concerns, even if they do not meet EU or national merger control thresholds

March 31, 2021

On March 26, 2021, the European Commission (EC) published the findings of its recent evaluation of procedural and jurisdictional aspects of European Union (EU) merger control. The key result is a change in the EC's policy regarding merger review referrals from EU Member States to the EC. Under the new Guidance on the referral mechanism set out in Article 22 of the EU Merger Regulation (Article 22 Guidance), in certain circumstances, the EC will accept case referrals from Member States *even if the transaction is not reportable in that Member State* under its national law.

The policy change is aimed at capturing transformative transactions in nascent markets—particularly in the tech and pharma sectors, including so-called killer acquisitions, that otherwise would not be subject to merger control at all—either at the EU or the Member State level. This type of transaction also has been a recent focus of the US and other competition authorities outside Europe. The policy change will broaden the de facto application of EU merger control law and create additional legal uncertainty for certain transactions, although the practical impact of the policy change remains to be seen. It may bring EU practice closer to that in the United States, where the antitrust agencies fairly commonly review transactions that are not reportable under the Hart-Scott-Rodino Premerger Notification Act.

Background

Under the EU Merger Regulation (EUMR), the EC has original jurisdiction to review transactions that meet the rather high sales/turnover thresholds set out in Articles 1(2) and 1(3) EUMR.[1]

[1] Under these tests, the target needs to have an EU-wide turnover of at least EUR 250m (Article 1(2) EUMR) or EUR 100m (Article 1(3) EUMR).

However, if these thresholds are not met, the EC can nevertheless review a transaction in two scenarios:

- According to Article 4(5) EUMR, the *parties may request a referral to the EC* if the transaction is reportable under the national competition laws of at least three Member States.
- According to Article 22 EUMR, *Member States may also request a referral to the EC* if a transaction (i) affects trade between Member States and (ii) threatens to significantly affect competition in the Member State(s) making the request.

If a Member State requests an Article 22 EUMR referral, the EC must investigate whether the legal requirements of Article 22 EUMR are met and, if so, it has administrative discretion whether or not to accept the referral request.

In the past, Article 22 EUMR has not been used often, with fewer than 40 cases referred to and accepted by the EC under Article 22 since the adoption of the EUMR. The vast majority of these referrals were requested by competition authorities in Member States with rather low notification thresholds, such as the German Federal Cartel Office, the Austrian Competition Authority, and (before Brexit) the United Kingdom's Office of Fair Trading/Competition and Market Authority, and concerned transactions related to (at least) European Economic Area (EEA)-wide markets that raised potential competitive concerns in a number of Member States. As it notes in the new Article 22 Guidance, the EC had developed a practice of discouraging referral requests under Article 22 from a Member State where the transaction did not meet the Member State's own jurisdictional criteria for review (though such referral requests are legally permissible under Article 22 EUMR).

The new Article 22 Guidance

The new Article 22 Guidance changes this policy. The EC now states that it will encourage and accept referrals in cases where the referring Member State ***does not*** have jurisdiction over the case under its own national law but where potential competition concerns arise under the criteria of Article 22.[2] The Article 22 Guidance explains which categories of cases might fall within this category.

The main motivation for this policy change is the EC's view that there are gaps in merger enforcement as regards acquisitions of firms that do not generate enough revenue to satisfy EU or Member State notification thresholds, but may play or develop into playing a significant competitive role in the relevant market.[3] The Article 22 Guidance expressly mentions transactions in the digital economy and in sectors, such as pharmaceuticals, where innovation is an especially important

[2] Article 22 Guidance, para. (11).
[3] Article 22 Guidance, para. (9).

competitive parameter.[4] Thus the Article 22 Guidance has the same goal as recent changes in German and Austrian merger control law that introduce a transaction-value threshold in their respective national merger control regimes in order to capture transactions that do not meet applicable revenue thresholds. The thinking behind this is that where a company attracts a high valuation even though it is not yet profitable or even generating revenue, this may be a sign that the target is viewed as a disruptive or highly innovative future force in the relevant market.

The EC will analyze the two-pronged legal requirements of Article 22 and exercise its discretion with the aim of closing gaps that had allowed some so-called killer acquisitions to go unreviewed in Europe.

i. Effect on trade between Member States. In analyzing whether a transaction affects trade between Member States, the EC will consider in particular factors such as the location of (potential) customers, the availability and offering of the products or services at stake, the collection of data in several Member States, or the development and implementation of research and development (R&D) projects whose results, including intellectual property rights, if successful, may be commercialized in more than one Member State.[5]

ii. Significant effect on competition. The Member State requesting a referral is required to demonstrate that, based on a preliminary analysis, there is a real risk that the transaction may have a significant adverse impact on competition, and it therefore deserves close scrutiny.[6] For purposes of assessing cases in the referral request, the EC will consider, inter alia, factors such as:

- the elimination of an "important competitive force,"[7] including the elimination of a recent or future entrant, or that the merger involves two important innovators;
- the reduction of the ability or incentive of a competitor to compete, including by making their entry or expansion more difficult or by hampering their access to supplies or markets; or
- the ability and incentive to leverage a strong market position from one market to another by means of tying or bundling or other exclusionary practices.[8]

iii. Exercise of discretion. Finally, in exercising its discretion regarding referral requests in cases where the transaction is not notifiable in the referring Member State(s), the EC will look primarily for transactions where the turnover of at least one of the undertakings concerned does not reflect its current or future competitive significance. As noted, this resembles the approach of the German

[4] Article 22 Guidance, para. (9).
[5] Article 22 Guidance, para. (14).
[6] Article 22 Guidance, para. (15).
[7] See, e.g., EC, Guidelines on the assessment of horizontal mergers, para. (37) and (38). Please also see most recently ECJ, judgment of 28 May 2020, T-399/16 - CK Telecoms UK Investments v Commission, para. (155) et seq. concluding that the EC's analysis of the "important competitive force" standard was insufficient.
[8] Article 22 Guidance, para. (15).

and Austrian competition authorities in their interpretation of the respective transaction-value tests.[9] This would include, for example, cases where the target:[10]

- is a startup or a recent entrant with significant competitive potential that has yet to develop or implement a business model generating significant revenues (or is still in the initial phase of implementing such business model);
- is an important innovator or is conducting potentially important research;
- is an actual or potential "important competitive force";
- has access to competitively significant assets (such as raw materials, infrastructure, data or intellectual property rights); or
- provides products or services that are key inputs/components for other industries.

As part of its assessment, the EC may also take into account whether the transaction value in terms of consideration is particularly high compared to the current turnover of the target.[11]

Procedural aspects

Under Article 22, Member States must request a referral within 15 working days after the date on which the transaction was either notified or, if no notification is required, was "otherwise made known to the Member State." The latter date is the one on which the Member State has sufficient information to make a preliminary assessment regarding the transaction and the referral, which will be difficult for merging parties to predict in advance.[12]

The Article 22 Guidance notes that third-party complainants may inform the EC or Member State competition authorities about transactions that, in their opinion, could be a candidate for a referral under Article 22.[13] Moreover, the EC may inform Member States about transactions that it believes meet the criteria for a referral and may encourage a Member State to request a referral.[14] However, the EC retains discretion as to whether or not to accept a referral.

If a referral is requested, the EC notifies all 27 EU Member States and the three EEA Member States (Iceland, Liechtenstein, Norway) about the request, and those countries may decide to join the request within 15 working days. After that period has lapsed, the EC has 10 working days to decide on whether to accept the request.

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[9] See Guidance on Transaction Value Thresholds for Mandatory Pre-merger Notification (Section 35 (1a) GWB and Section 9 (4) KartG), available here.
[10] Article 22 Guidance, para. (19).
[11] Article 22 Guidance, para. (19).
[12] Article 22 Guidance, para. (28).
[13] Article 22 Guidance, para. (25).
[14] Article 22 Guidance, para. (26).

Key implications

This policy change broadens the circumstances in which transactions may be reviewed at the EC level. It removes the de facto certainty that has existed to date that transactions that do not meet any EU or Member State notification threshold will not be reviewed by a competition authority in the EU. Acquirors or merging parties will now need to evaluate the risk of a potential referral request under the Article 22 Guidance for what are potentially competitively controversial transactions, even where the entities involved are not yet generating significant revenues in the EU.

The policy change therefore creates some uncertainty that is similar to that for non-reportable transactions in the United States. Parties to potentially controversial non-reportable transactions will need to consider the risk of an investigation by the EC, especially if there are potential complainants—e.g., customers, competitors or disappointed competing bidders for the target.

This legal uncertainty is addressed in part in the Article 22 Guidance:

- The EC states that the fact that a transaction has closed does not preclude a Member State from requesting (and the EC from accepting) an Article 22 referral.[15] However, the EC will, in its exercise of discretion, take into account the time elapsed since closing. Moreover, while analyzing potential competitive effects on a case-by-case basis, the EC states that it generally would not consider a referral appropriate when more than six months have passed after the closing of the transaction.[16] Particularly given the short time limits noted above for Member States to request referrals, this may prove to be a significant divergence from the practice in the United States, at least where a transaction is publicly known. In contrast to the EC's announced intention in the Article 22 Guidance, US authorities can and sometimes do challenge transactions (including seeking unwinding) long after a transaction has closed.
- Second, if the transaction already has been notified in one or several EU Member States that did not request a referral or join such a referral request, the EC is unlikely to accept a referral request, although it will make its decision based on all relevant circumstances, including the extent of the potential competitive harm and the geographic scope of the relevant markets.[17]

Going forward, it will be interesting to see how the Article 22 Guidance is applied and which types of transactions will be caught in practice. Acquirors of a company that is active in a highly

[15] Article 22 Guidance, para. (22).
[16] Article 22 Guidance, para. (21). If closing was not in the public domain, this period of six months would run from the moment when material facts about the transaction have been made public in the EU.
[17] Article 22 Guidance, para. (22).

innovative, R&D-driven sector, or that may control key inputs or intellectual property, will be well advised to take the new Article 22 Guidance into account in their merger control analysis.

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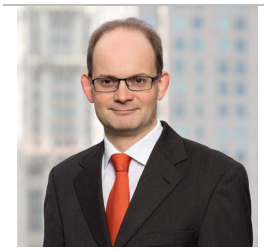

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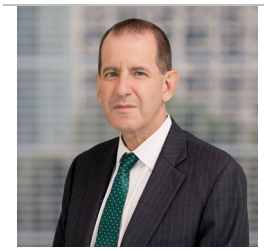

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