Antitrust, Competition, and Economic Regulation Quarterly Newsletter

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Contents

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Indonesia's competition authority reforms organizational structure and procedural law

On 1 July 2019 the Indonesian Competition Authority, Komisi Pengawas Persaingan Usaha (KPPU), reformed its organizational structure in order to gear up for a more efficient enforcement. As part of the organizational reform, KPPU established the Directorate of Economics, the Directorate of Competition Policy, and the Directorate of Competition Advocacy and Partnership (Small Medium Enterprise/SME) under the Deputy of Research and Advocacy. KPPU's Directorate of Merger & Acquisition and the Directorate of Partnership (Small Medium Enterprise/SME) Supervision were also restructured under the Deputy of Law Enforcement.

A few months earlier, in April, the KPPU issued Regulation No. 1 of 2019 on Monopolistic and Unfair Business Practices Case Handling Procedure (New Regulation). Commentaries by stakeholders are split between the good and the bad of the New Regulation as well as how it will it change the landscape of the competition law enforcement in Indonesia.

Restoring the possibility of obtaining a commitment decision

The most interesting part of the New Regulation is how it restored a procedure similar to the "commitment decision" under European Union competition law.

Although it is actually not an entirely new feature (the previous KPPU Regulation No. 1 of 2006 on Case Handling Procedure already had this commitment procedure, which, however, was subsequently removed in 2010) it shows that the current KPPU leadership is keen to use a variety of tools to restore effective competition in the market in an efficient manner, rather than merely increasing fines.

Qualification of evidence

After KPPU was closely scrutinized by the courts, practitioners, and academics in the past on how it looks at pieces of evidence, the New Regulation lays out a framework of how the evidence should be submitted and/or presented in the proceedings before it. Interestingly, circumstantial evidence is now clearly defined as "leads" (*petunjuk*), a form of admissible evidence. Throughout the history of competition law enforcement in Indonesia, courts have been split on whether to allow circumstantial evidence because this is not conventionally recognized under Indonesian laws.

It's not flawless

The New Regulation removed a number of "rights of defense" of the companies subject to a KPPU proceeding, which were previously provided in the KPPU Regulation No. 1 of 2010 on Case Handling Procedure, although some of those rights were retained in different sections of the New Regulation.

The New Regulation was also ambiguous on "site visit." Under the New Regulation, it is still unclear whether the KPPU Investigators could use the "site visit" provision to conduct an unannounced inspection or whether that provision can only be relied on by the Panel of KPPU Commissioners to clarify matters being examined in a hearing.

Although only published in April, this New Regulation was actually promulgated on 4 February 2019 and has been in effect since then. Therefore, all ongoing investigations which started earlier this year should have applied the New Regulation.

Conclusion

The new KPPU leadership is progressing towards fully reforming its organisation. We have the draft amendment of the Competition Law in the pipeline, which failed to be finalized before the general election and will invite even more commentaries with the newly elected Congress, as well as the draft amendment of the Supreme Court Regulation on Appeal Procedure.

Come what may, we expect more antitrust enforcement actions by the current KPPU leadership.

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U.S. Department of Justice foreshadows criminal investigations into antitrust violations in public procurement

Japanese companies involved in U.S. public procurement should be aware: The Department of Justice (DOJ) Antitrust Division (Division) has publicly announced that it is prioritizing investigations of criminal antitrust violations in the procurement process.

At a press conference announcing the plea agreements and indictment of two South Korean companies, Makan Delrahim – the Assistant Attorney General of the Division – explained that “[o]ne of the Antitrust Division’s top priorities is to protect the US government and tax payers.” Delrahim also said that the fuel supply investigation may spur investigations into other types of military supply around the world and that the Department of Defense (DOD) has “brought other matters to” the attention of the Department of Justice (DOJ). The top criminal antitrust official at the Division, Deputy Assistant Attorney General for Criminal Enforcement Richard Powers, echoed Delrahim’s statements at the American Bar Association (ABA) white collar conference where he identified public procurement cases as a priority for the Division’s criminal program.

The Division recently announced that two companies have agreed to plead guilty as part of an ongoing investigation into bid rigging and fraud on DOD fuel supply contracts for U.S. military bases in South Korea. The Division simultaneously unsealed an indictment charging seven individuals with violating criminal antitrust laws as well as committing fraud against the federal government. To date, five companies have pleaded guilty as part of the Division’s probe into these DOD fuel supply contracts.

Penalties for violating criminal antitrust laws in the United States are steep. Companies face maximum fines of US$100 million. In addition to criminal fines, the DOJ can pile on treble damages under both Section 4a of the Clayton Act and the False Claims Act (FCA) when the government is the victim of criminal antitrust conduct. For example, one of the companies that pleaded guilty in the fuel supply investigation – GS Caltex – has agreed to pay a total of US$104.17 million to the government in order to resolve the matter: US$46.67 million in criminal fines, US$14.88 million to settle the civil antitrust claims, and US$42.62 million to settle the FCA claims.

For individuals, the penalties are also severe. In addition to fines of up to US$1 million, individuals face imprisonment of up to 10 years. Foreign individuals are not protected from the consequences of indictment. The Division has previously extradited indicted non-U.S. citizens from countries such as Canada and Germany. The current administration also appears willing to consider extraditing individuals. In the recent fuel supply case, while Delrahim did not go into detail about the extradition process, he did say that the DOJ is exploring “every option for bringing these [indicted] individuals to the US” and has been in communication with the Korean Ministry of Justice “about access” to the individuals. According to Delrahim, the DOJ anticipates “full cooperation” with the South Korean authorities. The United States and Japan have a bilateral extradition treaty, on which U.S. authorities could rely to pursue extradition of any Japanese nationals indicted for such conduct.

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The Antitrust Division announces landmark policy shift to credit robust corporate compliance

"An ounce of prevention is worth a pound of cure." Assistant Attorney General Makan Delrahim (Delrahim) for the Antitrust Division of the U.S. Department of Justice (the Division or DOJ) called on the words of Benjamin Franklin as he detailed a historic change to the DOJ leniency program. While the Division has traditionally encouraged companies to report cartel activity by awarding the first company to report a violation with leniency, it has given minimal credit to defendants at either the charging or sentencing stage for corporate compliance programs.

That changed 11 July when Delrahim announced sweeping changes to the Division's approach to incentivizing compliance, including awarding credit at charging for compliance programs and permitting prosecutors to proceed by Deferred Prosecution Agreements (DPAs) against early cooperators that have effective compliance programs. In conjunction with these changes, the Division published for the first time ever a guidance document for companies detailing how antitrust compliance programs will be evaluated in criminal antitrust investigations.

The Division's new policy: Reward and incentivize corporate compliance

In the past, the Division has relied on its leniency program to incentivize companies to self-report cartel activity. Under its leniency program, the first company to self-report antitrust violations was immune from prosecution, while other members of the cartel would at minimum be required to plead guilty and pay fines. While early cooperators could receive a penalty reduction, only the first whistleblower received the benefit of immunity from prosecution. The Division's belief that effective compliance programs are those that allow the company to claim leniency underscored its winner-takes-all approach. Under this policy, DPAs for effective compliance programs were essentially unattainable. Delrahim announced that companies may now be credited at both the charging and sentencing stage for robust compliance programs. This fundamental shift provides avenues for credit and deferred prosecution even if a company was not first to disclose cartel activity under the leniency program.

The Division also published guidance for companies in support of this new policy. This document and Delrahim's remarks demonstrate an effort by the Department of Justice to update their outlook on compliance and reward companies for investments in effective compliance policies that can prevent antitrust violations before they occur. Prior to this release, guidelines had never been available for companies to consult when creating or evaluating antitrust compliance programs. The guidance contains two sections detailing how compliance efforts will be assessed by the Division. The first section explains how prosecutors should evaluate compliance programs at the charging stage and provides a list of factors used to determine the effectiveness of the program. The second section outlines how companies may receive credit at the sentencing stage for effective compliance programs through Sentencing Guidelines.

The Division may defer prosecution of companies with qualifying programs

DPAs allow for charges to be deferred and eventually dismissed by prosecutors provided that companies comply with the conditions of the DPA. Unlike the rest of the Department of Justice, the Division has been hesitant to use tools such as DPAs for fear that it would dilute the strength of its immunity program. However, in May 2019 the Division entered into a DPA with Heritage Pharmaceuticals in recognition of its cooperation with its investigation. The Heritage case appears to be a precursor of the Division's recently announced policy.

Under the new policy, companies can be rewarded for preexisting compliance programs at the charging stage. This new approach will allow prosecutors to proceed by DPA when relevant factors, including the adequacy and effectiveness of a company's compliance program, weigh in favor of doing so. In an evolution from its previous rationale that anticompetitive conduct is indicative of a larger problem at a company, the Division now views incentivizing compliance as a way to reduce enforcement activity and minimize harm to consumers and shareholders.

The guidance asks three fundamental questions in regards to compliance programs: "(1) Is the program well designed?; (2) Is it being applied earnestly and in good faith?; and (3) Does it actually work?" These questions get at several factors highlighted in the guidance document for prosecutors to consider when analyzing antitrust corporate compliance programs, including the design and comprehensiveness of the program, the culture of compliance within the company, and reporting mechanisms, among others.

While an excellent starting point for companies, Delrahim emphasized that the factors are not a checklist and will not automatically safeguard a company from liability. At the outset, prosecutors will question the effectiveness of the program, how promptly the violation was reported, and the extent to which company leaders were involved.

Three ways compliance programs receive credit during sentencing

If a DPA is deemed inappropriate, compliance efforts may still be credited at the sentencing stage. In his remarks, Delrahim detailed three ways in which antitrust compliance could affect companies during sentencing. First, an "effective" corporate compliance program could lead to a three-point score reduction under the Sentencing Guidelines. Second, a compliance program may help determine the appropriate fine to recommend under the Sentencing Guidelines. Last, a compliance program may affect whether the Division recommends probation and the appointment of an external monitor. Prosecutors will evaluate compliance programs on a caseby-case basis according to the new guidance issued by the Division. Prosecutors will consider not only the compliance program as it existed at the time of the offense, but will also consider what changes were implemented to address the antitrust violation.

Companies that prioritize catching antitrust violations through effective compliance programs, and working closely with authorities should they occur, may take advantage of the benefits of the Division's new policy. Companies will be incentivized to work with the Division and implement effective compliance programs, and in turn the Division will strengthen this incentive by recognizing and rewarding these efforts.

A tense balance: Incentivizing leniency applicants while rewarding compliance programs

In the past, the Division was concerned with providing incentives beyond leniency for corporate compliance programs. The Division feared that companies would rebuff leniency in favor of waiting for the government to initiate an investigation and then attempt to reap the benefits of its corporate compliance program. When announcing its new policy, the Division was adamant that the changes in the Division's policy do not spell an end to the leniency program. While taking questions, Delrahim reaffirmed the Division's commitment to the leniency program and said that it will continue to award the "ultimate credit" of a non-prosecution agreement under its leniency program to only the first company to report. Despite this rhetoric, there is tension between providing incentives beyond leniency for corporate compliance and encouraging self-reporting. In developing its guidance, the Division has not completely separated its assessment of a company's compliance program from the Division's leniency program. Its guidance specifically notes that "early detection and self-policing are hallmarks of an effective compliance program and frequently will enable a company to be the first applicant for leniency under the Division's Corporate Leniency Policy." The Division will consider both whether the compliance program uncovered the underlying violation and whether the company quickly self-reported the conduct when making a charging decision. The new policy also notes that the "Sentencing Guidelines are clear that a sentencing reduction for an effective compliance program does not apply in cases in which there has been an unreasonable delay in reporting the illegal conduct to the government." The Division will consider whether and when the company applied for a leniency marker under the Division's Leniency Policy when making its sentencing recommendation.

If a company is the first to self-report its reward is obvious: immunity from prosecution. For the second and third company to self-report – or the company that reports only after the government initiated an investigation – the reward is still less clear. The Division appears to be saying that as long as the company quickly self-reported due to its compliance program that a DPA or sentencing reduction may be an option. What is not clear is how quick is quick enough. If the Division holds leniency as the benchmark for expeditious reporting, this "new" policy may provide minimal additional benefit. If the Division is more lax in its interpretation, then companies may indeed receive benefits for adequate compliance even if they did not report in time to receive leniency.

Companies should consider re-evaluation of compliance efforts with an eye to the guidelines

These latest changes in the Division's approach to antitrust enforcement highlight a shift toward rewarding companies that are serious about their compliance programs. While the Division has reaffirmed that the leniency program remains the "ultimate credit" for immunity, companies involved in a criminal antitrust investigation may now have the opportunity to be credited for robust compliance programs that are well designed and effective in catching cartel activity. In light of these new changes companies should consider re-evaluating their compliance programs and, if necessary, consulting experienced outside counsel to align their program with the updated guidelines from the Department of Justice.

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Neither fish nor fowl – China's supreme court proposes new framework for resale price maintenance

In the last week of June 2019 a copy of a groundbreaking court ruling emerged on social media in China – the order by the Supreme People's Court (SPC) in the case between Yutai *Technology Feed (Yutai) and the Hainan Price Bureau.*

The order provides a direct answer to the question of whether or not the Chinese antitrust authorities bear the burden to prove the anticompetitive effects of companies' resale price maintenance (RPM) conduct. China's highest court found that they do not.

Background

The case started with an investigation by the Hainan Price Bureau, a local affiliate of the then, antitrust authority with jurisdiction over anti-competitive pricing conduct, the National Development and Reform Commission. In its investigation, the Hainan Price Bureau found that Yutai (as the supplier of fish feed) had a clause in its contracts with distributors which stipulated that the distributors had to follow the "guiding prices" set by Yutai in their resale to third parties. A deviation from those prices would give Yutai the right to withdraw benefits from the distributors. The Hainan Price Bureau found this arrangement to amount to RPM.

At the same, it was clear in the administrative procedure before the Hainan Price Bureau that Yutai had not enforced the clause in practice. On that basis, the Hainan Price Bureau concluded that Yutai had entered into, but not implemented, a RPM agreement in violation of Article 14 of the Anti-Monopoly Law (AML) and fined the company RMB 200,000 (around US$ 30,000).

Yutai appealed the Hainan Price Bureau's decision before the Haikou Intermediate People's Court, which annulled the decision on the ground that the authority had not proven that the RPM agreement had anti-competitive effects in the market.

The Hainan Price Bureau appealed the Intermediate People's Court judgment before the Hainan High People's Court. That court overturned the first instance judgment, holding that the Hainan Price Bureau was not required to prove anti-competitive effects.

Yutai further appealed against the Hainan High People's Court judgment (by way of request for retrial) before the SPC. The SPC issued the final ruling in the case with an order dated 18 December 2018.

SPC ruling

The SPC started its analysis on the substance in a broad way, referring to the goals of the AML and to several policy developments. It then laid out a general principle – making a distinction between agreements which are per se violations of the AML, and agreements whose violation can only be established after a detailed analysis. The court listed price fixing, output restriction, and market partitioning as examples of per se violations. In turn, the court found a detailed analysis to be required for agreements "other than the agreements where the per se illegality principle is used." The court further mentioned the following factors to be used in the detailed analysis: the specific market conditions, the change of market conditions before and after implementation of the agreement, and the nature and effect of the agreement.

After these initial, somewhat theoretical explanations, the SPC went closer to the key issue of the case – whether a showing of anticompetitive effects is required for an RPM finding.

The SPC first held that RPM is a typical vertical agreement which often has both pro and anticompetitive effects.

The court then found that the Chinese marketplace as such is not yet fully developed and the market's self-healing function is still weak. Against this background and taking into account that China is still at the beginning of its antitrust enforcement history, the court held that it was not appropriate to require the antitrust authorities to make a full-blown investigation and complex economic assessment in each RPM case. Doing so would greatly increase costs and decrease the efficiency of antitrust enforcement. In the SPC's view, thiswould not be in line with the current needs of China's antitrust regime.

As a result, the court found the antitrust authorities are not required to prove that an RPM agreement restricts competition. On the contrary, the onus is on the company under investigation to prove the absence of a restriction of competition or the applicability of the exemption clause (Article 15 of the AML, which lists certain pro-competitive or social factors such as technology improvement, product quality enhancement, environmental protection, etc.).

Applying these principles to the case at hand, the SPC found that Yutai had failed to provide sufficient evidence that its conduct did not significantly restrict competition in the market. The court ruled that the first-instance-finding that Yutai's scale of operations and market share showed the lack of anti-competitive effects was not supported by evidence and indepth analysis, hence erroneous. Even though the Hainan Price Bureau had accepted in the administrative procedure that Yutai had not implemented the RPM clause, the SPC held that the clause would still have the potential of restricting competition. In the court's view, the analysis of whether an agreement restricts "potential" competition is different from an analysis of the agreement's effects or the actual harm suffered by a market player.

Although the above reasoning would have allowed the court to stop its analysis there, it continued by distinguishing the Yutai case from prior judgments by lower courts, in particular the Shanghai High People's Court's judgment in *Rainbow v. Johnson & Johnson*. In that case, the Shanghai court had required plaintiffs in private antitrust lawsuits to prove the anticompetitive effects of RPM conduct as a precondition for a successful claim. In contrast, in Yutai, the SPC explicitly ruled that the standard of proof for administrative litigation (i.e., challenging the antitrust authorities' decisions) differs from that for civil litigation. According to the SPC, the reason is that a plaintiff in a civil lawsuit has to prove the actual damage suffered, an analysis closely related to the question of anti-competitive effects.

As a final point, the SPC noted the recent institutional reform and creation of the State Administration for Market Regulation (SAMR) with its unified antitrust enforcement powers in spring 2018, and found that SAMR should issue guidance to market players on vertical agreements.

Comments

The Yutai order is one of the few antitrust rulings by China's highest court. Its impact is significant. The SPC attempted to give guidance to the antitrust authorities and the lower courts on the substance of AML enforcement.

In Yutai, the SPC "got its hands dirty" going out to clarify the law in an area where there has not been detailed guidance on how to interpret the AML. It did so by refining the substantive antitrust analysis for examining agreements under the AML, by way of allocating the burden of proof and using presumptions which were not explicitly written into the law.

In the ruling, the SPC attempted to overcome the divergence between authority decisions and lower court judgments on what is required to bring a successful RPM case. Its reasoning suggests a compromise between two positions – that RPM is per se illegal (with no possibility of rebuttal), and that the antitrust authorities would need to conduct a comprehensive rule of reason analysis. In essence, the SPC found that RPM is subject to a rule of reason analysis, but the burden is on the company targeted in an administrative procedure to prove the absence of anti-competitive effects.

The reasons for the SPC's findings were quite clear. Using somewhat different language, the court seemed to suggest that the relative immaturity of the Chinese market (given that China started transitioning from a planned to a market economy only a few decades ago) means over enforcement may be more acceptable than under-enforcement at this stage. The SPC implied that an effects analysis for each RPM case would impose an excessive administrative burden on SAMR and its local offices, given the significant manpower shortage of the SAMR antitrust teams – at least at the central level in Beijing.

In Yutai, the SPC also laid out a benchmark for the effects analysis that is required for an RPM case. In the administrative procedure, even the Hainan Price Bureau had accepted that Yutai had not implemented the RPM clause. On that basis, Yutai argued that the lack of implementation means there were no negative effects on competition. Possibly to bypass that argument, the SPC found that a showing of a potential restriction of competition is sufficient. Future cases will show whether or not the court set a very low benchmark for effect analyses for RPM and possibly other cases.

The Yutai ruling is also significant beyond the narrow RPM question. Indeed, the SPC proposed to follow the per se rule of reason dichotomy of types of agreements in an almost identical way to the concepts as they are known on the international stage. In a way, the court came in to fill a void left open by the AML and its implementing rules, and to align AML enforcement with international practice.

Given the SPC's pro-active suggestion to SAMR to issue enforcement guidelines on vertical agreements, this may not be the last time the SPC intervenes if it believes the authorities fail to provide sufficient guidance.

For companies doing business in China, the Yutai ruling is a double-edged sword. On the upside, the ruling explicitly confirms RPM is subject to a rule of reason analysis, which in principle allows a showing of the conduct's procompetitive effects (by reference to factors such as low market shares, negative impact of freeriding by distributors, new market entry, etc.).

On the downside, once the RPM obligation on distributors is evidenced (through contractual clauses or otherwise), the burden is on the company to justify why the RPM arrangement does not restrict competition. Yet there is little guidance as to what justifications will be accepted by SAMR and its local offices. Arguing justifications "in defense" has always been a difficult endeavor in antitrust proceedings, in China and beyond. The stance of SAMR and its predecessor body, in practice, was that RPM is essentially per se illegal. A change in the enforcement culture and the attitude of the regulators is needed as much as a change in the text of the law. Hopefully, the Yutai ruling will bring about that change, and give companies involved in RPM investigations enough confidence to forcefully argue their case before the antitrust authorities.

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Illegal parking?

On 27 June 2019, the European Commission (Commission) announced it had fined Japanese camera and printer manufacturer, Canon, €28m for partially implementing its 2016 acquisition of Toshiba Medical Systems prior to the transaction being notified to the Commission and, as a result, before it had been formally given competition clearance. The focus of concern was the use of a so-called 'warehousing structure' – a two-step process during which the target company is temporarily "parked" with an intermediary buyer with the intention, the Commission claims, of circumventing EU merger control rules (rules requiring merging parties to notify and suspend implementation of their transactions pending approval).

The Commission's actions may come as no great surprise to some in that they confirm the Commission's long-held view that warehousing structures risk violating the EU rules governing mergers. Indeed, this point was made explicit when the Commission issued an updated *Consolidated Jurisdictional Notice* in 2008 – in particular, confirming that such transactions should be viewed as one single concentration with the intermediary stage merely being the first step towards implementation of the concentration.

This view, however, sits somewhat at odds with the findings of the EU Courts, which have previously confirmed the legality of such arrangements on the basis that the intermediary entity does not necessarily acquire 'control' over the warehoused company or assets. This potential discrepancy in views will no doubt become the focal point of Canon's anticipated challenge before the General Court – the essential questions being:

- To identify circumstances in which a 'concentration' is deemed to be 'implemented' within the meaning of Article 7(1) EU Merger Regulation (EUMR); and (as part of this).
- Whether the intermediary warehousing could be viewed as an action which contributes to, and is necessary for (ie is not merely "ancillary or preparatory") the change in control of the target (as per the Court of Justice's ruling last year in Ernst & Young) and, as such, forms the first step in implementing the concentration.

Merger control – procedural gun-jumping

Article 7(1) EUMR requires parties acquiring control of a business in a qualifying transaction (a so-called concentration with an EU dimension) to notify their transaction to the Commission for approval. The provision also prohibits the transaction from being implemented before it has been approved by the Commission – infringing conduct otherwise known as 'gun-jumping'.

Such procedural gun-jumping typically involves conduct falling short of actually taking formal ownership over a target's shares and assets and, instead, often entails more subtle measures that might be construed as prematurely transferring control over the target to the purchaser. The obligation to suspend the closing of a qualifying transaction exists regardless of whether or not the proposed merger creates potential substantive competition concerns – and the fact that a transaction may then receive competition clearance does not protect it from any potential prior violation of the standstill obligation.

Strict enforcement against procedural breaches of merger control rules, in particular failure to observe the standstill obligation, is very topical at the moment – with the Commission and other competition authorities investigating and/or imposing significant fines for gunjumping in a number of high-profile cases. This includes the Commission's *Altice/PT Portugal* infringement decision, issued on 24 April 2018, which fined the Dutch telecommunications company Altice €124.5m for an alleged infringement of the standstill provisions.

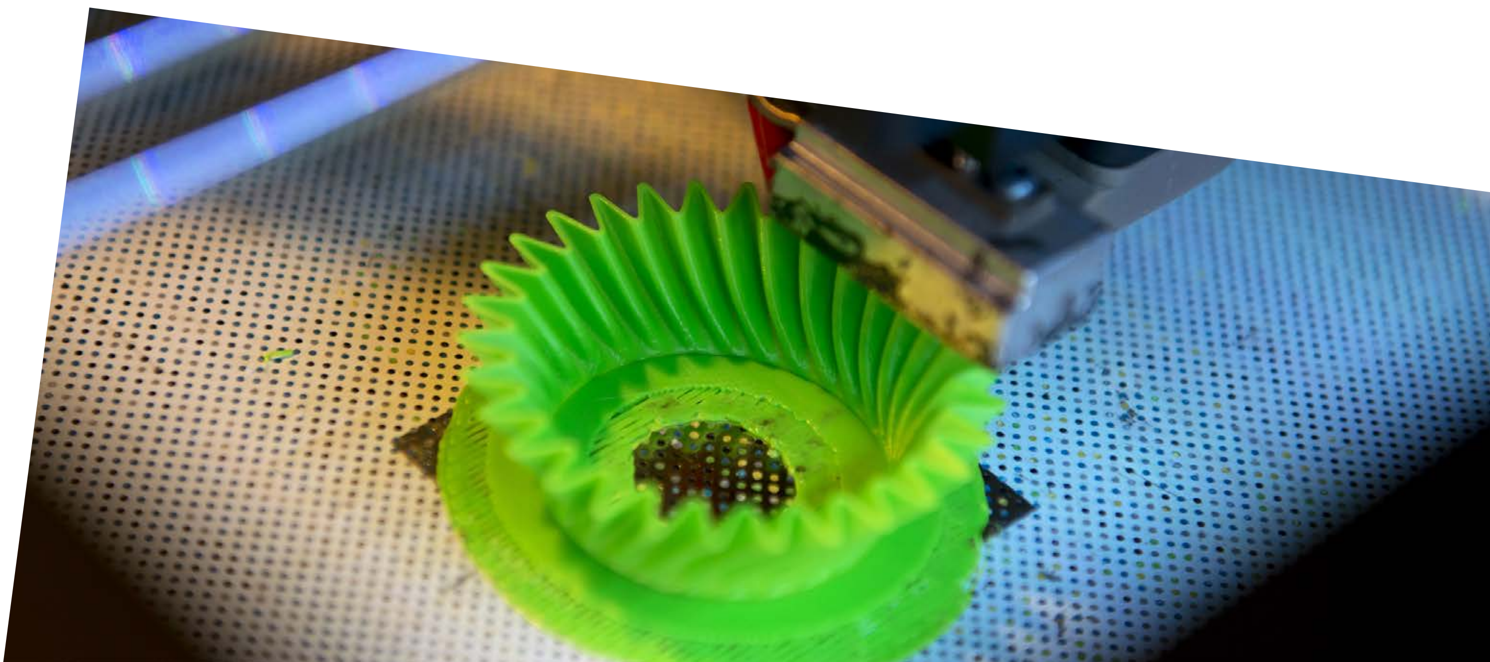
Background

In August 2016, Canon notified its planned acquisition of Toshiba Medical Systems to the Commission – with the Commission clearing the deal unconditionally the following month. However, before notifying the transaction to the Commission, there was an arrangement whereby an interim buyer purchased 95% of the target's shares for the nominal amount of €800. As part of this first step, Canon also paid €5.28 billion for the remaining 5% of the shares and share options over the interim buyer's stake (including a non-voting share providing it veto rights over any decision by the interim buyer to sell Toshiba Medical Systems to a different ultimate buyer). Only after the transaction was cleared by the Commission was the second step executed in which Canon exercised its share options and thus acquired 100% of the shares in Toshiba Medical Systems.

The parties had entered into this arrangement due to financial difficulties suffered by Toshiba Medical Systems' parent company, Toshiba, following its much publicised auditing issues. In short, Toshiba needed to close certain aspects of the transaction quickly to recognise financial benefits in a time-frame that would not accommodate prior receipt of all relevant merger control clearances. The warehouse structure was intended to facilitate an interim transaction so as to allow Toshiba to complete its sale of the medical system business promptly, without the need to wait for the Commission review process to be concluded.

Despite clearing the notified transaction, the Commission soon began looking into the arrangements entered into before the transaction was notified. Following the issuing of two Statement of Objections to Canon, the Commission concluded that the first step of the arrangement amounted to partial implementation of the transaction – insofar as it contributed to (and was necessary for) the ultimate change of control of the target at the second step of the process. In other words, the first and second steps in the transaction structure effectively formed a single concentration – and the first warehousing step was not, as intended, a separate stage at which the concentration with Canon did not arise.

On the basis of the above analysis, the initial measures should have been notified to the Commission for approval before being put into place. Canon therefore, according to the Commission, violated both the notification requirement and the standstill obligation under Article 7(1) EUMR.



End of the story?

Based on public statements, it seems likely that Canon will challenge the Commission's decision before the General Court. The focus there will then be on the main principles that can be distilled out of last year's Ernst & Young ruling handed down by the Court of Justice.

In its *Ernst & Young* judgment, the Court of Justice clarified that there is no breach of the standstill obligation on account of transactional activity pursued prior to a merger's clearance where such activity does not contribute to (and is not necessary in order to achieve) a change of control on a lasting basis of the target entity – and regardless of whether that activity results in market effects. Such "ancillary or preparatory" acts, whether or not they generate market effects, do not create a "direct functional link" with a proposed merger's implementation.

Accordingly, such arrangements are unlikely to undermine the objective of the EUMR's standstill provisions – namely, to exercise effective oversight over qualifying transactions *before* they produce lasting changes in market structure.

The Court of Justice's ruling was particularly helpful insofar as it re-centred the potentially amorphous category of behaviour constituting 'gun-jumping' around the central concept of a 'change of control' leading to the implementation of a concentration. In that regard, the Court of Justice's distinction between actions contributing to a change of control and mere preparatory actions is a useful delineation (at least in principle).

However, it will be interesting to see how this might be applied to the facts of the Canon case – in particular, whether the General Court agrees that the first warehousing step can be construed as 'partial implementation' of a notifiable concentration. In other words (and as governed by the principles identified in *Ernst & Young*), can the intermediary 'parking' of the business being sold be viewed as an action which contributes to, and is necessary for – rather than being merely "ancillary or preparatory" – a "change in control on a lasting basis" of the target entity?

Conclusion

The recent spate of gun-jumping investigations by various competition authorities underscores their determination to make compliance with the procedural merger rules a key enforcement priority, whilst also illustrating the risks companies face for failing to meet such requirements.

This most recent case also highlights the dangers involved in using a warehousing structure to facilitate a deal – despite the potential inconsistency that exists between relevant EU jurisprudence on the issue and Commission decisional practice. Indeed, even if arguably permissible under relevant EU law (and even if Canon were to be successful with its appeal before the General Court), global deals may nevertheless encounter difficulties justifying such an approach with other relevant competition authorities that also have jurisdiction to review (noting that Canon was also fined by a number of other authorities for this specific arrangement). In short, at least for large cross-border transactions, there remains a significant risk in pursuing such a strategy, notwithstanding commercial pressures that can arise to do so.

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Commission seeks interim measures for the first time in 18 years

On 26 June 2019, the European Commission announced that it has opened a formal investigation to determine whether US chipmaker, Broadcom, is abusing its allegedly dominant position in the markets for modem and TV chipsets through its imposition of exclusivity requirements on customers (amongst other alleged breaches of competition law). In parallel, the Commission issued a Statement of Objections notifying Broadcom of its intention to impose an interim measures order restraining its allegedly exclusionary practices pending conclusion of the investigation.

This is the first time in nearly two decades that such interim measures have been pursued by the Commission. It also comes at a time when the Commission is coming under pressure to ensure competition law enforcement is timely and effective, particularly in respect of fast-moving digital markets. Part of the challenge has been to determine whether existing enforcement tools are adequate for dealing with the issues arising with digitisation. The fact that the Commission turned here to an existing but much under-used power therefore marks this out as an interesting test case.

European Commission interim measures regime in antitrust cases

Under Article 8(1) of Regulation 1/2003, which codified precedent first set out in the 1980 European Court of Justice *Camera Care v European Commission case*, the Commission has the power to order interim measures on the basis of a prima facie finding of infringement where there is an urgent need to respond to a risk of serious and irreparable damage to competition. Broadcom marks the first time since the *IMS Health* case in 2001 (and the first time since the passing of Regulation 1/2003) that the Commission has sought to rely on these powers.

The Commission in *IMS Health* ordered IMS, which at the time was the leading supplier of pharmaceutical sales data, to license the use of its copyrighted data collection system to its competitors in Germany. IMS appealed to the Court of First Instance (now the General Court), which issued a temporary order suspending the interim measures pending the Commission's final decision. Two competitors of IMS unsuccessfully appealed the Court of First Instance's order to suspend interim measures to the Court of Justice. The Commission eventually withdrew the order in 2003, following from a substantive ruling in favour of IMS Health by a German court.

In its Statement of Objections issued to Broadcom last month, the Commission set out that Broadcom was likely to hold a dominant position in various modem and TV chipset markets and that certain agreements between Broadcom and some of its customers contain exclusivity clauses that may marginalise or eliminate competitors (and, in turn, stifle innovation in those markets). The Commission arrived at the preliminarily conclusion that an interim measures order is indispensable due to the risk of serious and irreparable harm to competition occurring before the end of its investigation. It reasoned that such measures are necessary to ensure the enforceability and efficiency of future decisions by the Commission following the end of the investigation. Broadcom now has the opportunity to reply to the Statement of Objections and attend an oral hearing in Brussels before the Commission can proceed to impose the interim measures.

Interim measures: A tool for dealing with challenges posed by the "new" economy?

The Commission has recently come under pressure, from both national competition authorities and academics, to make use of its powers to impose interim remedies, particularly in relation to the fast-moving digital economy. Similarly, in the UK the Furman Report commissioned by the Competition and Markets Authority also recommended increased use of interim measures as a means to ensure moreeffective competition law enforcement in digital markets.

The main concern raised by commentators is the length of investigations. On average, antitrust investigations take several years to conclude. By the time the Commission makes a final decision, it is argued that it may be too late as a means to address the antitrust issue in question because by then the affected market may have tipped in the infringing party's favour. In digital platform markets in particular, there is a risk that an incumbent may irreversibly change the market in its favour in a relatively short period of time.

As it stands, the extent to which the Broadcom matter reflects a broader change in the Commission's attitude regarding the use of Article 8 powers in antitrust cases is unclear. However, the Commission is following an approach championed by the French Competition Authority for some time. As far back as 2015, the President of the French Competition Authority, Mr Bruno Lasserre, argued that interim measures are especially appropriate in the digital economy. To this end, the French Competition Authority ordered interim measures against Google in January 2019 during its investigation of alleged anti-competitive practices directed at Amadeus, a directory enquiry services provider.

Giving weight to this view, Guillaume Loriot, the director responsible for digital telecoms and media at DG Competition in the Commission, said earlier this week that "antitrust enforcement must and does adapt to the challenges of the new economy, new practice and new conduct". In this context, he believed that "it is extremely important to be flexible and use the tools we have". In respect of Broadcom, he noted that the interim measures would prevent the market "tipping" in Broadcom's favour during the course of the investigation.

Moving forward: A lower threshold for invoking Article 8 powers?

Under the current framework, there is significant evidential and procedural burden that must be met by the Commission in order to justify imposing interim measures. In particular, it is a hard standard to prove that conduct is causing, or will cause, serious and irrevocable damage to competition. According to a Commission official, this has dissuaded the use of interim measures in the past and attempting to do so can actually slow down investigations.

Compounding this is the high risk of judicial challenge. Most Commission interim order decisions have been appealed, with defending appeals in IMS Health having proved costly to the Commission. It is expected that Broadcom will challenge the Commission's decision were the Commission to proceed with the order. Such considerations have led various commentators to advocate reducing the threshold for invoking Article 8 powers. For example under UK competition law, the equivalent threshold was amended by the Enterprise and Regulatory Reform Act 2013 from "serious and irreparable damage" to "significant damage". It remains to be seen whether EU competition law will follow suit in lowering the bar to the use of this regulatory enforcement tool.

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SAMR's triple guidance on antitrust enforcement

On 1 July 2019, the State Administration for Market Regulation (SAMR) made public three sets of regulations to implement China's Anti-Monopoly Law (AML):

- the Interim Regulation Prohibiting Monopoly Agreements (SAMR Agreements Regulation);
- the Interim Regulation Prohibiting Conduct Abusing Dominant Market Positions (SAMR Abuse of Dominance Regulation); and
- the Interim Regulation Preventing Conduct Abusing Administrative Rights to Eliminate or Restrict Competition (SAMR Administrative Monopoly Regulation).

The three regulations will enter into force on 1 September 2019.

The regulations contain a mix of substantive and procedural rules. In many ways, they represent continuation of the AML implementing rules issued by SAMR's predecessors as antitrust enforcement body, the National Development and Reform Commission (NDRC) and the State Administration for Industry and Commerce (SAIC).

A read-through of the three regulations reveals an attempt by SAMR to lay out similar rules for three of the four types of anti-competitive conduct targeted by the AML: anti-competitive agreements; abuse of a dominant market position; and abuse of administrative rights to restrict competition (often dubbed "administrative monopoly" conduct in China). Guidance on the AML's merger control provisions is provided in separate SAMR implementing rules.

Anti-competitive agreements

The SAMR Agreements Regulation contains 36 provisions. The procedural provisions make up the bulk of the regulation. These provisions focus inter alia on SAMR's jurisdiction, case delegation to its local offices, and supervision of the local work; complaints; the commitments process; and the leniency regime.

The substantive provisions in the SAMR Agreements Regulation put forward guidance on the various prohibitions for horizontal agreements listed in the AML – namely, various types of hardcore cartel conduct – and resale price maintenance as the only vertical agreement. The guidance is largely similar to that in the prior NDRC and SAIC regulations, with no big surprises.

Similarly, the SAMR Agreements Regulation restates the prior SAIC guidance on the concept of "concerted practice," laying out the factors to be considered: unity in market conduct; meeting of minds or information exchange; reasonable (counter-) explanations; and seemingly objective factors such as market structure, status of competition, and market change.

The SAMR Agreements Regulation also contains guidance on how to operate the AML's "catch-all clause" for finding anti-competitive agreements not explicitly listed in the AML. The regulation sets out a few general factors, such as the degree of competition in the market; market shares; impact on prices, market entry etc. but – unlike an earlier draft – does not provide a market share safe harbor.

Interestingly, the guidance on how to use the AML's exemption provision is quite limited. The regulation appears to view the exemption as a procedural mechanism (like a defense) rather than as a part of the substantive analysis.

Abuse of dominance

The SAMR Abuse of Dominance Regulation has 39 provisions. On the procedural front, the provisions are very similar to those of the SAMR Agreements Regulation.

From the substantive perspective, the SAMR Abuse of Dominance Regulation puts forward the most detailed guidance among the three regulations. First, it attempts to further flesh out the factors in the AML for finding dominance. For example, the regulation explains that market shares can be measured by reference to sales value, sales volume or "other norms."

Beyond the general guidance on the dominance assessment, the SAMR Abuse of Dominance Regulation contains specific points for the Internet sector and intellectual property rights (IPRs): for Internet and similar businesses, the dominance assessment can look at the industry specificity; business models; user numbers; network effects; foreclosure effects; technological characteristics; market innovation; and data control and processing, and any associated market power. In the IPR space, countervailing power (likely to mean the licensee's bargaining position in a cross-licensing context) is a relevant factor.

Interestingly, the SAMR Abuse of Dominance Regulation also includes new detail on "collective dominance," a rarely used concept in the AML. Largely in line with international practice, the regulation proposes to assess the market structure; transparency in the market; the degree of homogeneity of products; and the parallelism of the companies' conduct as relevant factors in the collective dominance assessment.

Second, the SAMR Abuse of Dominance Regulation goes into quite some detail on the types of abusive conduct. The regulation addresses each of the prohibitions in the AML and – on many aspects – provides additional guidance, going beyond the AML and the prior NDRC and SAIC regulations. For example:

- One of the benchmarks for excessive pricing is the dominant company's own prices in another geography with the same/similar market conditions (one of the criteria which NDRC had used in the River sand case).
- The proposed cost benchmark for predatory pricing is average variable cost.
- A refusal to grant access to an "essential facility" is subject to a somewhat different test than arefusal to supply other products or services.
- "Restrictive dealing" (similar to "exclusive dealing" known on an international basis) can be achieved directly or indirectly – in line with SAMR's sanctioning of the minimum purchasing volumes, take-or-pay clauses, and discounts in the Eastman case in April 2019).
- Unreasonable charges other than price can amount to unlawful imposition of unreasonable conditions, an offense similar to tying.
- A long list of items (including for example different warranty periods) can be used to assess whether there is discrimination between two transaction parties and there is additional guidance as to when two businesses are comparable enough to be examined under the discriminatory treatment clause in the first place.

Third, perhaps most notably, the SAMR Abuse of Dominance Regulation goes at great length to describe the circumstances of "valid reasons" justifying potentially abusive conduct – both in the individual provisions for each type of abuse and in a separate, additional stand-alone provision.

Fourth, similar to the SAMR Agreements Regulation, the SAMR Abuse of Dominance Regulation puts forward criteria for operating the AML's "catch-all clause" for finding new types of abuse of dominance, explicitly requiring that SAMR prove the anti-competitive effects of the conduct.

Administrative monopoly

With 25 provisions, the SAMR Administrative Monopoly Regulation is the shortest of the three regulations.

On the procedural side, the SAMR Administrative Monopoly Regulation naturally differs from the other two regulations, as the AML does not empower SAMR to impose sanctions on the infringing administrative organ but only to issue recommendations to the organ's hierarchically superior body on how to rectify the anti-competitive conduct. However, bearing in mind this significant procedural difference, it seems the SAMR Administrative Monopoly Regulation attempts to find as much common ground as possible with the SAMR Agreements Regulation and the SAMR Abuse of Dominance Regulation, on aspects such as jurisdiction, case delegation, complaints and other procedural steps.

The substantive provisions of the SAMR Administrative Monopoly Regulation largely follow the structure of the AML, providing some more detail on what specific government actions can be deemed to be anti-competitive. The main focus of the provisions is to regulate two types of anti-competitive government conduct – exclusivity for certain producers/service providers to the detriment of others, and restrictions to the free movement of goods, services and investment within China.

Perhaps the most interesting feature of the SAMR Administrative Monopoly Regulation is not what it says, but what it does not say: there is no direct reference to the "Fair Competition Review System," a policy originally established outside the AML framework which aims to screen government rules, policies and actions for their compatibility with market competition.

Takeaways

The procedural aspects in the three regulations are similar. To a large extent, the procedural provisions are not ground-breaking. Admittedly, the rules on jurisdiction by SAMR's provincial offices and case delegation between offices are key to future AML enforcement, as the antitrust human resources at central SAMR in Beijing are very limited. However, those rules are not new, but were decided late 2018 when SAMR issued its Notice on Anti-Monopoly Enforcement Delegation.

In contrast, a new feature in the three regulations is the push for additional publicity and transparency in SAMR's decision-making process. In particular, the regulations mandate publication of all final decisions – seemingly including settlement decisions and decisions recommending rectification of administrative monopoly conduct, politically quite a sensitive topic in China.

There is also an attempt at consistency in terms of substantive rules. For example, both the SAMR Agreements Regulation and the SAMR Abuse of Dominance Regulation call for an effects-based analysis for new types of anticompetitive agreements and abuse of dominance under the AML's "catch-all clauses."

However, the attempt to streamline the set of regulations is not present throughout. For example, there is a noticeable difference among the three regulations on how to "justify" potentially anti-competitive conduct: while there is a lot of detail in the SAMR Abuse of Dominance Regulation, the SAMR Agreements Regulation contains very little, and the SAMR Administrative Monopoly Regulation virtually no, guidance (despite the fact that the implementing rules for the "Fair Competition Review System" provide for justification possibilities, by way of exception, for anticompetitive government actions).

Overall, although a different format for the implementing rules – such as guidelines with case studies or hypothetical examples – might have provided more clarity for market players, the three SAMR regulations provide some welcome guidance as to how the authority will interpret and enforce the AML going forward.

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Vietnamese competition law reloaded

On 1 July 2019, the amendments to Vietnam's Competition Law came into effect. The amendments have the potential of marking the beginning of a new era.

The revision of the Competition Law is in line with a push of economic liberalization by the government over the past few years. Efforts to increase business sector transparency, combat corruption, streamline licensing and investment procedures, and strengthen the protection of intellectual property and other private property rights have allowed Vietnam to advance 13 spots in the 2019 Index of Economic Freedom as compared to the previous year. However, as with all things in Vietnam, the success of the amended Competition Law will depend on how the law will be implemented in practice.

With the draft implementing decrees not yet enacted and the new competition authority still in the process of being set up, it is too early to assess the real impact of the amended Competition Law on market players in Vietnam.

Background

Originally, the Competition Law was enacted in 2004. Two authorities were responsible for enforcing the law: the Vietnam Competition Authority and the Vietnam Competition Council. In the years since its enactment, a range of cases have been brought under the Competition Law against anti-competitive agreements, abuse of dominance, and in the merger control area. Nonetheless, the authorities were subject to important constraints, in particular their limited human resources, so the cases were not very numerous.

In June 2018, the National Assembly, Vietnam's legislative body, approved the first amendments to the Competition Law since its original enactment in 2004. Importantly, the amended Competition Law mandates a new authority to be created. But on the substance and procedure of the law, the amendments represent more of a gradual change, rather than a complete revamp.

Anti-competitive agreements

Chapter 3 of the revised Competition Law deals with anti-competitive agreements. Similar to the EU, the Competition Law follows a two-step approach: prohibition and exemption.

On the substantive law front, Articles 11 and 12 of the amended Competition Law set out which types of agreements are prohibited and which standard is used to find the illegality. In turn, Article 14 lists the criteria that a potentially anti-competitive agreement needs to fulfill to be exempted.

Reorganizing the complex provisions somewhat, Articles 11 and 12 in essence put forward four categories of agreements which are subject to different standards of review:

1. Certain types of cartel agreements – price-fixing; customer or market allocation; and output limitation – are per se illegal.
2. Other types of horizontal agreements (between competitors) – such as technology restrictions; imposition of unrelated conditions; or refusal to deal with third parties – are subject to a "rule of reason" analysis which examines whether the agreements in question have a substantial anti-competitive effect in the market.
3. All vertical agreements covering the same content as those explained in 1) and 2) above are subject to the "rule of reason" analysis.
4. Certain types of agreements – bidrigging; preventing third parties to access the market; and eliminating third parties from the market – are per se prohibited for all businesses (seemingly beyond the horizontal and vertical agreements concepts).

Except for this last category of agreements in 4), any agreement can be exempted if certain arguably pro-competitive effects are shown. The benchmarks for the exemption assessment seem similar to EU competition law and international practices – for example, the promotion of technical progress or improvement to quality standards. However, the other benchmarks – agreement on conditions unrelated to pricing for contract performance, product delivery and payment, and the increase of the competitiveness of Vietnamese companies on the international market – seem to go beyond EU competition law. Perhaps Chinese competition law – with a similar exemption for exporting businesses – may have been a reference point here.

On the procedural law front, the Vietnamese exemption rule is also similar to EU competition law, but to that in force before 2004. As pre2004 in Europe, an agreement can only be exempted after Vietnam's National Competition Commission (NCC) has examined and approved the parties' application for exemption. The parties cannot implement the agreement before the NCC's decision.

Since the NCC is expected to have relatively limited resources, at least at the beginning of its mandate, the exemption possibility may have limited practical importance for market players. Instead, businesses will probably need to conduct self-assessments to make sure their agreements cannot be deemed to be anticompetitive under Articles 11 and 12.

The new Competition Law also introduces for the first time a leniency regime to allow cartelists to self-report and assist the NCC in exchange for full or partial immunity from sanctions. A leniency application must satisfy certain conditions in order to benefit from the leniency regime. In particular, the leniency applicant must:

- Come forward to the NCC before a formal investigation is launched.
- Provide all evidence of the breach of law, thereby adding sufficient value to the NCC for dismantling the cartel.
- Cooperate fully with the NCC during the entire investigation.
- Not have acted as the ring-leader of the cartel.

Only the first three whistleblowers in a cartel are eligible for relief under the leniency regime, with the first entitled to full immunity and the second and third eligible for a reduction in fines of 60% and 40% respectively.

Although the effectiveness of the leniency regime will need to be tested during the implementation of the revised Competition Law, lawmakers hope that it will incentivize cartelists to come forward on their own initiative to help authorities detect and sanction cartels.

Abuse of dominance

Similar to the provisions on anti-competitive agreements, Chapter 4 on abuse of a dominant position may have been inspired by European competition rules. For example, the "collective dominance" presumptions – for various unrelated market players – seem inspired by German competition law.

At the same time, Vietnam's amended Competition Law has its own distinct flavor. As a starting point, the law prohibits abuses not only by dominant companies but also puts forward special rules for companies in a "monopoly position." In addition, unlike many foreign antitrust laws which generally revolve around 50% market share as a benchmark or rule of thumb, the amended Competition Law has presumption of dominance at 30% market share.

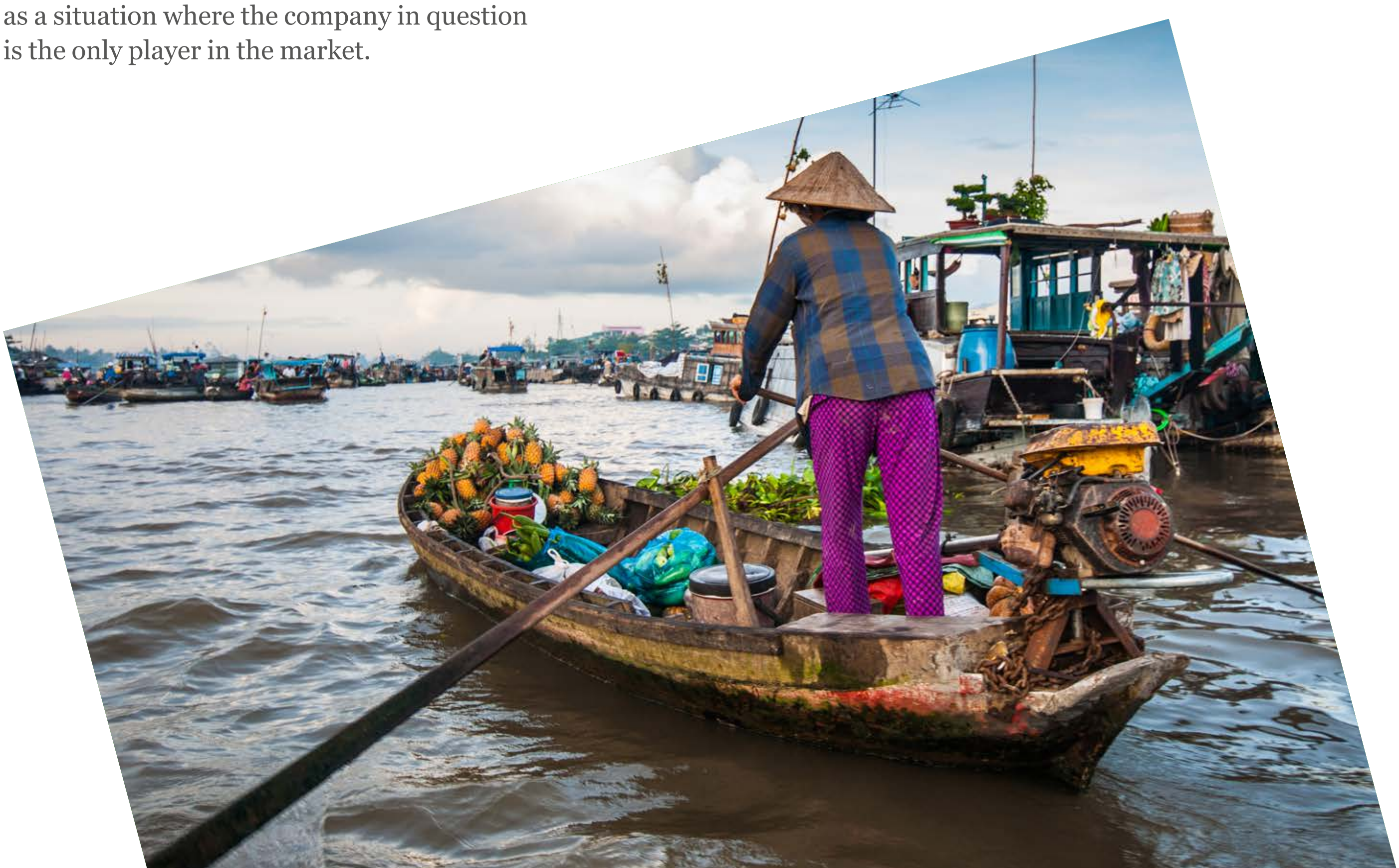
In addition, in line with international competition rules, dominance can also be shown through "softer" factors such as financial strength; barriers to entry; control over sources of supply; technological prowess; etc.

A monopoly position, in contrast, is defined as a situation where the company in question is the only player in the market.

If a company is found to be dominant, it is prohibited from:

- Engaging in predatory (i.e., below-cost) pricing.
- Imposing unreasonable resale prices or resale price maintenance.
- Restricting production or distribution or limiting technology development.
- Discriminatory treatment.
- Imposing unrelated conditions.
- Preventing other companies from market entry or expansion.

A company in a monopoly position is prohibited from engaging in the same type of conduct as listed above – with the exemption of predatory pricing. In addition, a monopolist cannot impose unfavorable conditions on customers or unilaterally modify existing contracts without justification. In other words, such a company cannot impose conditions to the disadvantage of customers.



Merger control

Merger control is one of the areas where the Competition Law amendment is perhaps bringing the biggest change. Before the amendment, companies would only need to notify their deals if the parties to the deal exceeded a combined market share of 30%. Post-amendment, there will be a number of thresholds triggering notification obligations:

- The value of the parties' combined assets in Vietnam.
- The parties' combined revenues in Vietnam.
- The transaction value.
- The parties' combined share in the relevant market.

If any of the thresholds are triggered, a filing will be required and closing cannot take place before clearance is granted by the NCC.

However, while the amended Competition Law sets out these new thresholds, it does not provide details on how to operate – as such, the law itself does not put forward numbers for the thresholds. The details are to be hammered out in implementing decrees. However, as of today, the implementing decrees have not yet been enacted.

A prior draft decree on the interpretation of certain provisions of the Competition Law put forward VND 3,000 billion (roughly US$128.2 million) for combined assets and revenues, VND 1,000 billion (around US$42.7 million) as transaction value, and 20% combined market share as numeric thresholds. The draft decree also proposed that the transaction value threshold would not apply to transactions outside Vietnam.

We will see in the coming weeks or months if these numbers are confirmed for the thresholds and if each threshold has a proper "local nexus" – that is, if all or at least two parties to the transaction have a sufficient link to Vietnam. For example, a key question will be whether the combined asset and revenue thresholds can be triggered by a single party, or whether it is necessary for at least two parties to have assets or revenues above certain thresholds.

Irrespective of the final outcome of the determination of the filing thresholds through the implementing decree, it is already clear now that the amended Competition Law can represent a paradigmatic shift in Vietnamese merger control. Indeed, filing thresholds based on the value of assets, revenues, and transaction value are more objective, hence measurable, benchmarks than market shares (which depend on a prior definition of the relevant market, a less objective, more case-by-case benchmark).

The amended Competition Law also sets out the basic procedural framework for the merger control analysis. On this point, the law is close to international practice, providing a two-stage review: a "preliminary assessment" phase lasting 30 days, and a further "formal assessment" phase lasting 90 days (with a possibility to extend for another 60 days). After the preliminary assessment, the NCC makes one of the following decisions:

- The procedure stops right there (without a formal assessment) and the transaction can be implemented.
- The transaction must undergo the formal assessment.

Under the amended Competition Law, the NCC also has the power to "stop the clock" when issuing requests for information (RFI). However, the law in principle limits the number of RFIs the NCC can issue to two. In other jurisdictions, the antitrust authorities may issue well over two sets of RFIs in complex cases. Hopefully this limitation will not stand in the way for an efficient handling of a case for both the NCC and the parties.

Unfair competition

Article 45 of the amended Competition Law prohibits certain "unfair competition practices." The conduct prohibited by this provision includes trade secret infringement; forcing business partner not to deal with third parties; discredit competitors by spreading false information; disrupting the legitimate operations of competitors; unlawful baiting practices; and predatory pricing.

In most foreign jurisdictions, these types of prohibitions would not be considered part of the "antitrust regime" in the strict sense. Interestingly, before January 2018, China had similar provisions as those set out above, mixed together with antitrust rules in a narrow sense, in the country's Anti-Unfair Competition Law. After January 2018, the antitrust rules were eliminated from that law.

In contrast, in Vietnam, the NCC will police violations of these unfair competition practices in parallel to the rules on anti-competitive agreements, abuse of dominance, and merger control.

New authority

The amendment of the Competition Law brings about an organization change. Instead of the two prior authorities (the Vietnam Competition Authority and the Vietnam Competition Council), a single authority – the NCC – will have jurisdiction for enforcing the Competition Law.

The NCC will not be an independent body but, like its predecessors, be inserted within the Ministry of Industry and Trade.

Reminiscent of its two-authority origin, the NCC will have a bifurcated character, with the Competition Investigation Agency (CIA) as the "working-level" body and the decision-making level, with 15 members at the top. The NCC members are officials of the Ministry of Industry and Trade and other ministries, as well as experts and scientists.

That said, the Competition Law also provides for smaller groups including individuals to lead the cases. As such, the President of the NCC and the head of the CIA play important roles to organize and push forward cases. In addition, a so-called "Anti-competitive Settlement Council" is to be set up by the NCC President, consisting of three to five NCC members, and tasked to decide on agreements and abuse of dominance cases. This way of "delegating" decision-making to smaller groups or individuals is similar to the regime in place under the original Competition Law enacted in 2004.

Conclusion

The amendment of the Competition Law represents a gradual change of Vietnam's competition regime. Still, if the NCC is staffed properly and competition law and policy receives broad support within the Vietnamese government and society, the amendment may well work as a "re-set," providing the starting point for more active antitrust enforcement going forward.

The actual effectiveness of the amended Competition Law will depend on a number of factors, such as what kind of authority the NCC will be (for example, how many staff it has and who its leaders are). Once established, we will need to see which priorities the NCC sets; how it applies the law to State-owned enterprises; if and how it cooperates with foreign antitrust authorities; etc.

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UK to create a 'Digital Markets Unit'

On 10 June 2019, the outgoing UK Prime Minister confirmed that the UK government will move forward with a proposal for a new 'Digital Markets Unit'. In her speech at the launch of London Tech Week, Theresa May noted that the author of the report recommending establishment of such a body, Professor Jason Furman, will be charged with setting up the specialised unit and advising the government on its implementation.

Furman Report on digital markets

The Furman Report ('Report', published in March 2019) was far reaching in its proposals and, it would seem, inspired some of the views put forward by the Chair of the Competition and Markets Authority (CMA), Lord Tyrie – in a letter before publication of the Report and more recently in a speech and a subsequent appearance before the House of Lords. Overall the Report's panel of experts determined that the competition rules as they currently stand (antitrust/behavioural review and merger control/transactional review) are inadequate for dealing with the (often novel) concerns that arise in modern digital markets and that UK competition policy needs to be updated accordingly.

Notably, the Report concludes that large tech players face inadequate competition – with digital markets demonstrating high levels of concentration and tending to "tip" to a "winner" who takes most or all of the market. Combined with alleged under-enforcement in merger reviews (noting that five big tech players have made over 400 acquisitions in the last 10 years and implying that some of these deals should probably not have been allowed), start-ups and new entrants appear, in the panel's view, to face considerable challenges.

'Digital Markets Unit'

Amongst the specific proposals put forth in the Report to address some of these concerns is the creation of a new 'Digital Markets Unit'. This body would regulate platforms designated as having 'strategic market status' (a status that would also require such platforms to flag to the CMA all acquisitions they intend to make – regardless of whether the UK's jurisdictional thresholds for merger control are met). More specifically, the Report recommends that the

Digital Markets Unit:

- Establishes a digital platform 'code of conduct' for platforms that have been designated as having a 'strategic market status.'
- Pursues personal data mobility and systems with open standards where these will deliver greater innovation and competition.
- Uses 'data openness' as a tool to encourage competition (where necessary and proportionate to achieve its aims).
- Cooperates with a wide range of stakeholders but with powers to impose solutions and to monitor, investigate and sanction non-compliance.
- Is empowered to impose measures where a company holds a 'strategic market status' – with enduring market power over a strategic bottleneck market.
- Is resourced with the capability, specialist skills and funding required to perform its functions successfully.

A paper published recently by the Department for Business, Energy and Industrial Strategy (BEIS) confirmed that UK government has *"carefully weighed up the evidence and agree with the Digital Competition Expert Panel that there is a strong case for establishing a procompetition Digital Markets Unit, tasked with securing competition, innovation and beneficial outcomes for consumers and businesses in the digital economy"*. The UK government will later this year provide its analysis of Furman's recommendations as part of a broader competition "green paper" which intends to stimulate discussion.

It remains to be seen what the Digital Markets Unit will look like in practice and what the scope of its role and powers will be. Crucially, the Report refrained from recommending whether it should sit within an existing regulator (ie the CMA or the Office of Communications – Ofcom), or as a new standalone regulator. The CMA has expressed disagreement with the latter approach on the basis that this would dilute existing pools of expertise. Amelia Fletcher, who co-authored the Report, recently suggested that the Digital Markets Unit could go hand-in-hand with a proposed Online Harms Regulator.

International focus

These discussions come amid a flurry of developments and commentary, both in the UK and abroad, focused on digital markets. Competition authorities globally are grappling with questions about whether current enforcement tools are adequate for dealing with the challenges posed by digital markets. In short, they are confronted with the issue of how best to harness the clear benefits of digitisation (pro-consumer innovation, etc) whilst, at the same time, curbing what some see as the development of 'ecosystems' in which (it is alleged) large tech players derive significant competitive advantage and secure positions that appear increasingly unassailable.

Prominent critics and reformers (such as Lord Tyrie and Senator Elizabeth Warren in the US) have, in particular, described a tendency towards more concentrated markets in which a small number of tech players dominate – citing, for example that five tech giants alone reportedly have a combined market cap in excess of US$3.5 trillion (greater than the GDP of most advanced nations). It is their view that this level of concentration and corporate power (especially in dynamic tech markets which feature so prominently in modern life) not only has implications for properly functioning and competitive markets, but also for social cohesion and democracy.

The UK government itself acknowledges that the status quo might not be acceptable with the UK Chancellor, Phillip Hammond, recently suggesting that UK competition rules may no longer be "fit for purpose" in an age of increased digitisation. In his words, "the Furman review is really focused on the proposition that as the economy changes, the regulatory structures that we have in place have to change with them".

Brexit and policy priorities

This development in thinking about digital markets in the UK would appear to run up against new realities caused by Brexit. For example, just as the UK will be looking to assure global companies that the UK remains "open for business" despite its potential departure from the world's largest trading bloc, it is also sending out messages that could potentially chill investment in a post-Brexit economy (for example, openly considering whether UK merger control should move from a voluntary to a mandatory regime). Furthermore, the funding required to meet the identified challenges posed by digitisation comes at a time when most (if not all) government departments will be requesting additional financing to deal with the fallout from Brexit (especially in a 'no deal' scenario).

However (and despite the stark choices and complications brought about by Brexit as well as the inevitable strain on government resources), dealing with concerns about the operation of digital markets is clearly a UK government priority. Funds have apparently been earmarked for the creation of a Digital Markets Unit as well as the go-ahead for the CMA to undertake a 'market study' of the digital advertising market (as announced by Phillip Hammond in his Spring Statement).

Going forward – first stop, merger control?

The UK government's interest in digital commerce is multifaceted and clearly covers a range of issues from consumer protection concerns to conduct covered by the UK's competition law provisions. That said, it appears that there may be an initial focus on the operation of the UK's merger control regime.

On 3 June 2019, the CMA published a commissioned report by Lear, an economic consultant firm, which reviewed past digital sector merger decisions taken by the UK's Office of Fair Trading and the Competition Commission (the UK competition authorities prior to the CMA).

Publication of this report coincided with a speech on competition and the digital economy delivered by the CMA's Chief Executive, Andrea Coscelli, to the Organisation for Economic Cooperation and Development/G7 conference. Dr Coscelli's speech focused on the effectiveness of merger control in digital markets and emphasised that "evolution" rather than "revolution" was needed in terms of the tools used by the CMA in assessing mergers – noting that the Lear report shows "that there are incremental steps competition authorities can take to improve our ability to assess these mergers."

To this end, Dr. Coscelli considered that that Lear did not uncover any fatal flaws or gaps in the existing UK regime and that the CMA's focus going forward should, therefore, be on taking effective action "using our existing powers and tools". It remains to be seen whether such effective action would include the somewhat radical and, for companies undertaking transactions, potentially worrying idea floated by Lear of using 'dawn raids' in a merger context to gather greater evidence regarding the merging parties' future plans and views of the market(s). Nevertheless, the mere discussion of the idea reflects regulators' desire to have as complete a picture as possible when making their assessments and, in turn, underscores the growing emphasis and focus on internal documents in merger reviews.

To better understand how the CMA might take effective action using "existing powers and tools", Dr Coscelli announced the launching of a 'Call for information on digital mergers' with the intention of updating the CMA's Merger Assessment Guidelines (guidance which has not been updated since 2010 despite the substantial evolution and growth of digital markets). This consultation process is open until 12 July, with the expectation that input provided by stakeholders will help recalibrate the CMA's approach so that it is better able to assess and effectively deal with issues arising in digital markets.

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“Devices for avoidance” don’t avoid HSR penalties

On 10 June 2019 the U.S. Department of Justice (DOJ) Antitrust Division, acting at the request of the Federal Trade Commission (FTC), filed a complaint and proposed final judgment in the U.S. District Court for the District of Columbia, alleging that Canon Inc. (Canon) and Toshiba Corp. (Toshiba) violated the premerger notification and waiting period requirements of the Hart-ScottRodino Act (HSR Act), 15 U.S.C. §18a, in connection with Canon’s acquisition of Toshiba Medical Systems Corp. (TMSC), a subsidiary of Toshiba.

The final judgment imposed a US$5 million civil penalty, split evenly between Canon and Toshiba. Often, the DOJ and FTC impose penalties on the acquiring person only, but given the parties’ intent to circumvent the HSR notification rules, the agencies instead sought penalties against both companies for most of the full amount that could have been levied – approximately US$6.4 million – and required each to institute an HSR Act compliance program, which must include among other things at least two hours of HSR training for all relevant employees.

What is particularly significant about this matter is that, although the parties willfully evaded the HSR Act’s notification requirements, their motives for doing so were not anticompetitive. To the contrary, Toshiba was motivated by a desire to shore up its financial statements with the proceeds from selling TMSC, after it incurred a significant accounting charge and was forced to restate its earnings. The HSR Act provides the agencies with an opportunity to evaluate whether a particular transaction will harm competition before the transaction is consummated. However, even where the agencies would have cleared a transaction without issue, parties will still be held accountable for willfully depriving the agencies of the opportunity to investigate.

Transaction background

In Toshiba's case, after discovering long-running accounting irregularities during a 2015 independent investigation and facing financial difficulty, Toshiba determined it would need to sell TMSC and recognize the proceeds of the sale by the end of its fiscal year. Although Toshiba began the sale process in December 2015, it did not resolve the sale process with sufficient time to file premerger notifications and obtain the necessary clearances in various jurisdictions. See *Compl., U.S. v. Canon Inc.,* No. 1:19-cv-01680, ¶ 26 (10 June 2019). In March 2016 as it neared the end of its fiscal year on 31 March, Toshiba and Canon implemented a scheme to consummate the sale of TSMC to Canon while evading the notification and reporting requirements of the HSR Act.

Specifically Toshiba and Canon arranged for the creation of a special purpose company – MS Holding Corp. (MS Holding). Toshiba also created new classes of voting shares for TMSC and a "single non-voting share with rights custom-made for Canon, and options convertible into ordinary shares." Compl. ¶ 6. MS Holding then acquired the newly issued voting shares of TMSC for a nominal amount (US$900) well below the US$50 million (as adjusted) HSR size of transaction threshold (US$78.2 million at the time). Canon acquired both the nonvoting shares and the convertible options – the acquisition of which is generally nonreportable under the HSR Act (which applies to the acquisition of voting shares of corporations) – for US$6.1 billion (the value of TMSC). Canon issued a press release regarding the share acquisition and acknowledging that the acquisition was intended "to make TMSC a Canon subsidiary." Compl. ¶ 29. Approximately nine months later – and after complying with the HSR Act to report an acquisition of TMSC voting shares from MS Holding (not Toshiba) – Canon exercised its options and acquired the TMSC voting shares, thereby obtaining full control of TMSC through what appeared to be two independent transactions.

HSR Act prohibition on "devices for avoidance"

The HSR Act's implementing regulations specifically prohibit the use of "[a]ny transaction(s) or other device(s) entered into or employed for the purpose of avoiding the obligation to comply with the requirements of the [HSR] act." 16 Code of Federal Regulations § 801.90. These are known as devices for avoidance.

When the agencies conclude that a particular transaction structure is being used as a device for avoidance, they determine whether the parties have an HSR reporting obligation by evaluating the substance of the transaction. In this case, the DOJ alleged that there was no independent business reason for the transaction structure and that MS Holding bore neither risk of loss nor benefit of gain associated with TMSC because MS Holding "existed precisely to be bought out after Canon exercise[d] its options" and thus "had no incentive to maintain the long term viability of TMSC." Compl. ¶ 33. In other words, MS Holding was created and used to mask the true nature of the acquisition, which was intended to transfer complete ownership and control of TMSC from Toshiba to Canon. Accordingly, Canon's acquisition of TMSC was subject to the HSR Act's notification requirements, and the parties were noncompliant from the time Canon acquired the nonvoting shares until expiration of the waiting period associated with its HSR notification to report its proposed option exercise and resulting acquisition of TMSC voting shares from MS Holding – a period of approximately five months.

Key takeaways

The risk associated with noncompliance with the HSR Act's notification requirements is significant: the maximum current penalty is US$42,530 per day of noncompliance, and both the acquiring and acquired party alike may face steep penalties even for a first offense if the agencies determine that that offense was not inadvertent. This case highlights the importance of consulting experienced HSR counsel early in the process, even if the transaction does not appear to have any substantive antitrust issues. HSR counsel can advise whether a specific transaction structure could qualify as a device for avoidance (or otherwise constitute the transfer of beneficial ownership over the target) and therefore require the making of HSR filings and the observance of HSR waiting periods before closing. Moreover, if the parties wish to meet tight closing deadlines, and are not able to execute definitive agreements in time to file HSR notifications and observe the HSR waiting period before the desired closing date, parties may still be able to meet the desired closing date by filing HSR notifications off of a nonbinding letter of intent or term sheet before the definitive agreements are executed. In such cases, it is important to involve HSR counsel early in the process.

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ADG Insights: Foreign investment control in the European Union and its Member States

In recent years, several European Union (EU) Member States, as well as the EU itself, have reconsidered their approaches to foreign direct investment (FDI). An increasing number of European jurisdictions have introduced rules restricting FDI or have strengthened existing rules.

To date, 14 of the 28 Member States have adopted mechanisms to scrutinize FDI, ranging from screening procedures to partial or total prohibition of FDI in specific sectors. Among these countries are Europe's largest economies Germany, the United Kingdom, and France,[1] all of which recently tightened their FDI screening regimes. Even European countries that are traditionally recognized as the most open economies, such as the Netherlands and Switzerland, are in the course of or considering or adopting FDI regulations.[2] Furthermore, the EU itself has recently introduced FDI screening regulations for the first time, adopting a "framework for the screening of foreign direct investments into the Union".[3]

Albeit diverse in their nature and procedures, all of these mechanisms aim to address challenges raised by FDI into sectors deemed sensitive or strategic to national economies or national security. This particularly concerns companies active in the aerospace, defense, and government services (ADG) industry. National governments have traditionally kept a close watch on the ADG industry and the current trend is toward even tighter regulation. In the United Kingdom, for example, new provisions amending the Enterprise Act 2002 expressly expand the regulations to cover smaller businesses active in the military and dual-use sectors, and the advanced technology sector.[4] ADG companies should therefore pay close attention to the regulations in force when conducting cross-border transactions and assess their potential impact on the due diligence process and the timing of transactions. As the regulatory frameworks are subject to constant change, it is crucial to stay on top of those developments.

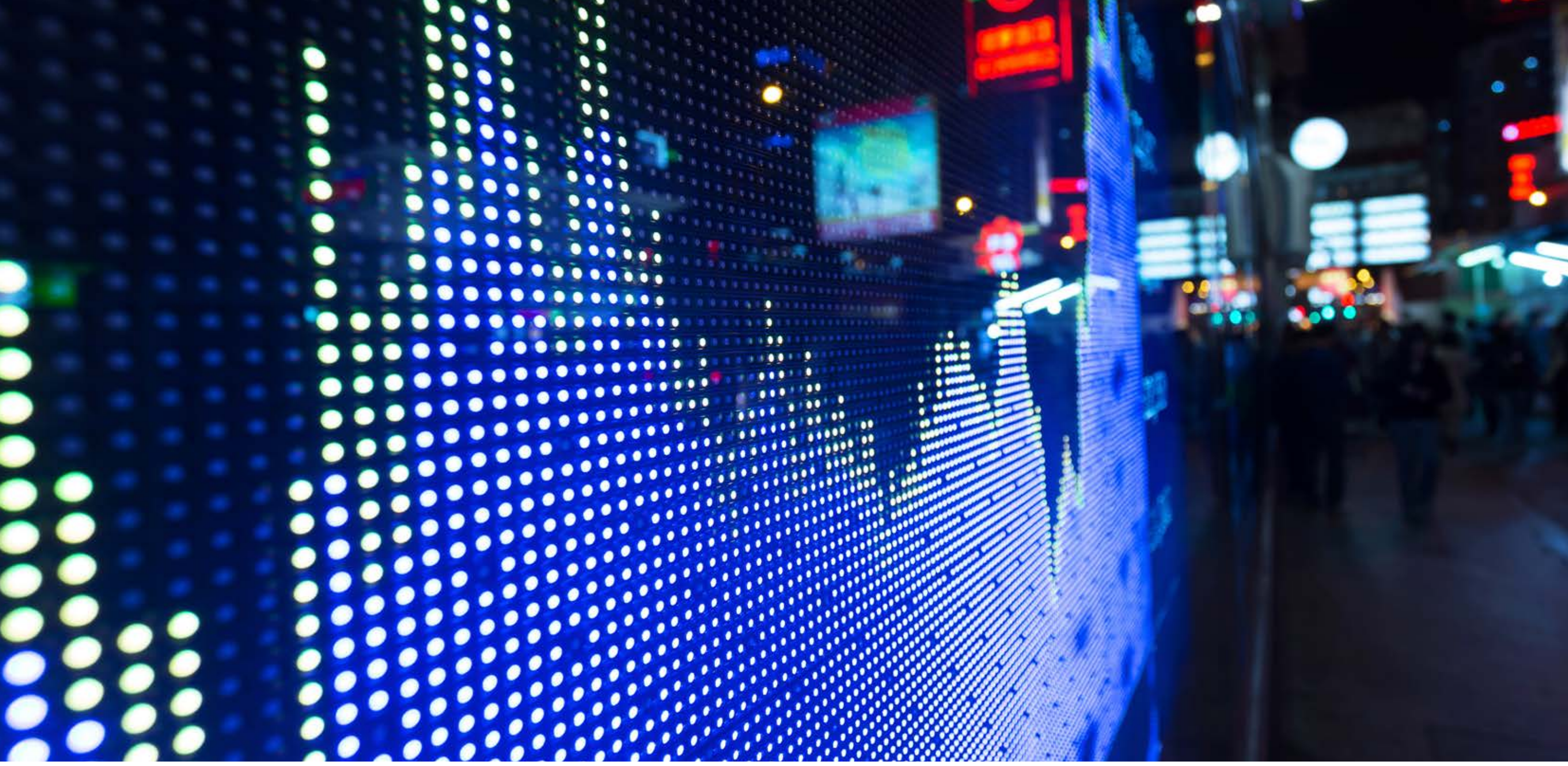
This article aims to provide (1) an introduction to foreign investment control; (2) an overview of the legal framework for FDI screening on EU level; and (3) a summary of recent developments in the area, an outlook on what to expect in the future, and recommendations for the mergers and acquisitions (M&A) process.

1. Background, applicability, and M&A implications of foreign investment control

a) Background and rationale for FDI screenings

The surge in takeovers of EU-based companies manufacturing key technologies and of strategic infrastructure assets by non-EU investors has raised concerns about the potential impact of these transactions on national security or public order. While globalization is leading to an increasing number of cross-border transactions, one of the main factors drawing regulators' attention is the involvement of more and more state-owned funds, enterprises, conglomerates, and private firms with close government links in such transactions.

Two political camps are facing each other in the dispute over the right regulatory response. While the free market-oriented side rejects or seeks to limit scrutinizing mechanisms as protectionist, the more interventionist camp welcomes such regulation. The latter camp is mainly driven by a fear that investments by state-affiliated investors are not market-based, but strategic efforts to facilitate, among other things, "know-how theft" with the goal of surpassing more advanced economies. The debate has considerably intensified since the beginning of the world economic crisis in 2008. In Western economies such as those in Europe, and even more in the United States, weight is shifting more and more to interventionist trade and market policies.[5] In contrast, emerging economies have historically been to a large extent closed to FDI and are now attempting to open their domestic markets to it.[6]



b) Relevance for the ADG industry

Of the sectors under regulatory scrutiny, the sector scrutinized most commonly is (and has traditionally been) military and defense, followed by the "critical infrastructure" sectors. The latter term can be defined as an asset, system, or part thereof which is essential for the maintenance of vital societal functions, health, safety, security, economic, or social well-being of people.[7] While definitions in indiv`such as the energy, water, telecommunications, health care, transport and infrastructure, and certain finance infrastructure sectors. Within the ADG area, airports are one example that could fall into this category.

Importantly, FDI screenings not only extend to situations where fully assembled products or facilities are in question, but are also used to scrutinize investments in companies that make spare parts and in subcontractors. This may under certain circumstances extend to the manufacturing of products as simple as screws if specifically designed for a use relating to other covered products. An example of this is the German Federal Government's decision in 2018 to block the proposed acquisition by a Chinese investor of Leifeld Metal Spinning, a German manufacturer of metal forming machines used in the automotive, aerospace, and nuclear industries, which did not itself produce or assemble vehicles, airplanes, power plants, or parts thereof itself.

1. Other Member States with FDI screening mechanisms are Austria, Denmark, Italy, Latvia, Lithuania, Hungary, Poland, Portugal, Romania, Spain, and Finland. The list can be retrieved on the European Commission's website under http://trade.ec.europa.eu/doclib/docs/2019/june/tradoc_157946.pdf. Our previous coverage of the list's publication is available under https://www.hoganlovells.com/en/blogs/focus-on-regulation/foreign-investment-control-on-the-rise-new-list-of-eu-member-states-fdi-screening-mechanisms.
2. The Swiss Federal Council has only recently blocked a motion to introduce foreign investment control. Documentation is available on the Federal Council's website under https://www.parlament.ch/de/ratsbetrieb/suche-curia-vista/geschaeft?AffairId=20183021 (only in German, French, and Italian). Meanwhile, the Dutch government is currently preparing certain regulations providing for FDI screenings for national security reasons to be introduced in the future. Assessments are made on a sector by sector basis, while legislation for the telecommunications sector is already underway.
3. See further to this below under (2).
4. New provisions, which came into force on 11 June 2018, introduced lower merger control thresholds for transactions in certain sectors. The target turnover threshold was reduced to as little as £ 1 million from previously £ 70 million). These revised thresholds are designed to provide the UK government with increased scope to scrutinize FDI and transactions that raise national security concerns. For further information, see our previous coverage regarding the topic here: https://www.hoganlovells.com/en/publications/new-uk-foreign-investment-screening-rules-come-into-force.
5. The recently published "Franco-German Manifesto for a European industrial policy fit for the 21st Century", which followed the Alstom/Siemens prohibition by the European Commission, is a notable example of this. Therein, strong support for the recently adopted European foreign investment screening framework as well as "tough national legislation as France and Germany already have in place" regarding FDI is advocated. The manifesto can be retrieved on the website of the German Federal Ministry for Economic Affairs and Energy under https://www.bmwi.de/Redaktion/DE/Downloads/F/franco-german-manifesto-for-a-european-industrial-policy.pdf?__blob=publicationFile&v=2. Our previous coverage of the matter can be retrieved under https://www.hoganlovells.com/en/blogs/focus-on-regulation/we-are-the-champions-france-and-germany-unite-to-revive-industrial-policy-at-european-level.
6. For example, China has recently introduced a new foreign investment law to promote FDI against the backdrop of increasing trade tensions with the United States. See our coverage regarding the matter here: https://www.hoganlovells.com/en/publications/the-foreign-investment-law-a-new-chapter-opens-for-foreign-direct-investment-in-china.
7. The full definition according to Article 2 of Council Directive 2008/114/EC of 8 December 2008 on the identification and designation of European critical infrastructures and the assessment of the need to improve their protection is as follows: "'critical infrastructure' means an asset, system or part thereof located in Member States which is essential for the maintenance of vital societal functions, health, safety, security, economic or social well-being of people, and the disruption or destruction of which would have a significant impact in a Member State as a result of the failure to maintain those functions."

c) M&A implications

Foreign investment control procedures share many commonalities with merger control procedures. In fact, the foreign investment review procedure is in some jurisdictions handled by the competent competition authority as an annex or similarly to merger control procedures. A notable example in Europe is the United Kingdom's Competition and Markets Authority (CMA). Since the Enterprise Act 2002 came into force, the UK government can formally intervene in cases caught by the UK merger control thresholds (and smaller transactions involving government contractors) where specified public interest considerations are engaged.

Furthermore, the regulatory impact of both merger control and foreign investment control on the transaction has to be assessed and the approach and timeline regarding both should be aligned in order to secure a smooth and timely closing of the transaction.

Figure 1: Impact of FDI screenings on M&A transactions

Procedural elements

- Are there any standstill obligations (i.e., is pre-approval required before closing)?
- Can the authorities impose specific obligations as a condition for pre-approval?
- Should risk shifting provisions be included in the share purchase agreement?
- Can the authorities rely on third-party consultations?
- Do anti-circumvention provisions apply?

Due diligence elements

- List of countries in which the target company is active or has subsidiaries.
- Market valuation of the target company (in local currency).
- List of sensitive activities conducted by the target company (e.g., national security/ safety; critical infrastructure; public interest).
- Relationship of the target company with local public entities.

Identifying how an FDI screening could impact the transaction structure is particularly relevant for the M&A process in ADG transactions. While the situation differs in each country, as a general trend four different schemes can be identified. Notification requirements are in place in most jurisdictions for the more critical investments in the fields of security and defense and critical infrastructure. For other areas, voluntary notification regimes exist that enable investors to obtain transaction approval by engaging proactively with the authorities. Finally, many jurisdictions also provide for the option of ex officio investigations into planned or closed transactions.

Figure 2: FDI screening categories

Voluntary notification	Mandatory notification in the area of critical infrastructure, certain export-controlled items, or certain IT systems	Mandatory notification regarding war weapons and arms	Ex officio (even post-closing) investigations by competent authorities

2. Foreign investment control at EU level

The EU has recently chimed in on the prevailing trend of FDI regulation, and on 21 March 2019 published Regulation (EU) 2019/452 (Framework Regulation),[8] establishing, for the first time, a common structure for the screening of FDI into the EU. It came into force on 10 April 2019 and will fully apply from 11 October 2020.

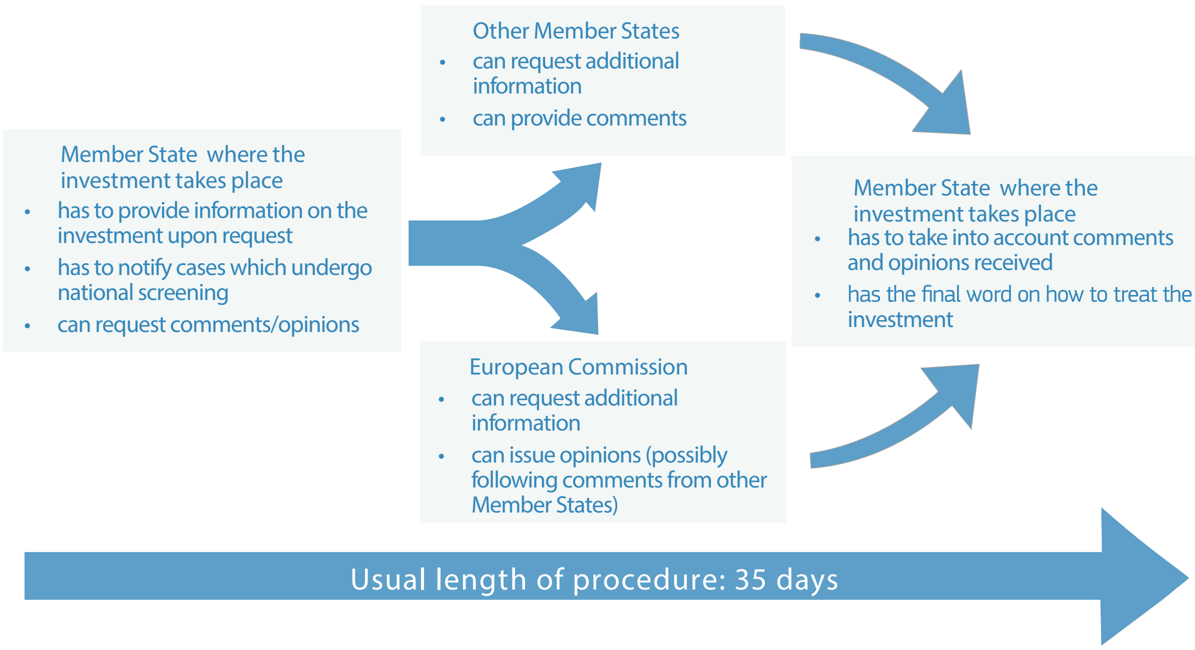
Unlike with the EU merger control regime, in the context of FDI screening the EU does not act as an overarching regulator holding supranational jurisdiction and issuing binding decisions. Member States retain the final say as to whether a specific investment should be permitted or not in their territories. Furthermore, the Framework Regulation does not attempt to harmonize Member State screening mechanisms or to create an EU-wide screening mechanism, nor does it impose an obligation on Member States to have in place a screening mechanism. Rather, it aims to enhance cooperation and increase transparency between Member States and the European Commission.

Main features of the framework include the following:[9]

- It introduces certain common principles for national screening mechanisms, such as transparency, non-discrimination, timeframes, confidentiality of information, and possibility for judicial redress.
- It creates a "cooperation mechanism" whereby Member States are required to exchange information (among themselves and with the Commission).
- One of its aims it to allow for enhanced cooperation through the exchange of any relevant information, such as the ownership structure of the foreign investor, the approximate value of the FDI, the products, services, and business operation of the foreign investor and the target company, etc.
- Furthermore, it allows the European Commission to issue non-binding opinions where security or public order might be affected and which have to be considered by the concerned Member State(s).
- Lastly, the framework aims at encouraging international cooperation on screening policies, including sharing experience and best practices as well as information regarding investment trends.

8. Regulation (EU) 2019/452 of the European Parliament and of the Council of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union.
9. A more detailed overview can be derived from our earlier coverage on the Framework Regulation here: https://www.hoganlovells.com/en/blogs/focus-on-regulation/new-eu-framework-for-screening-foreign-direct-investment.

Figure 3: Information exchange procedure pursuant to the Framework Regulation



(Source: European Commission, http://trade.ec.europa.eu/doclib/docs/2019/february/tradoc_157683.pdf)

In order to increase the visibility of FDI screening regimes, on 24 June 2019 the Commission published a list of FDI screening mechanisms notified by Member States, which shows that to date, 14 out of the 28 Member States already have mechanisms scrutinizing FDI in place.[10] As part of the Framework Regulation, Member States with an FDI screening mechanism in place are obliged to notify the Commission of such mechanisms.

3. Looking forward

In the coming years, we expect the number of European jurisdictions increasing scrutiny of foreign investment will grow. Authorities' review competences primarily grow by expanding the scope of applicability of the regulatory framework. Most commonly this happens by extending the review powers to additional sectors and by lowering thresholds – for example, the stake to be acquired in a target, which has recently been set as low as 10 percent for critical infrastructure and security and defense acquisitions in some jurisdictions, such as Germany. Parties to M&A transactions should carefully monitor such developments in their due diligence processes.

1. Europe

On a European level, it can be expected that the new EU Framework Regulation will have a significant impact on M&A transactions. First, and in line with the trend of recent years, it increases the likelihood of more Member States introducing FDI screening tools to level the playing field. Second, for those Member States that already have a screening mechanism, the new rules will likely impact both the timing and the substance of the assessment.

Member States will need to take comments from other Member States and the Commission into account. The additional "usual" timeframe of 35 days for the information exchange procedure regarding FDI screenings is likely to delay the national procedures and decouple the procedure from the shorter first phase merger control reviews in most Member States.

10. See above under footnote 1.

Furthermore, the criteria for concerns to be raised regarding the security or public order of Member States are too broad and not defined, leaving room for legal uncertainty in their applicability.

2. International context – CFIUS and FIRRMA

The current focus on foreign investment control in Europe mirrors developments across the world, including the recent U.S. Committee on Foreign Investment in the United States (CFIUS) reform. In August 2018, the Foreign Investment Risk Review Modernization Act (FIRRMA) was signed into law.[11] Among other things, it considerably expands the scope of "covered transactions" and the factors the CFIUS may consider when assessing security risks. The scope now includes purchases or leases of real estate in close proximity to sensitive U.S. government facilities and non-controlling acquisitions in U.S. businesses whose activities involve critical technologies, critical infrastructure, or sensitive personal data of U.S. citizens. The law extends the timelines for CFIUS investigations, introduces declaration procedures for expedited notifications, and makes declarations mandatory in certain cases such as critical technology. This is a fundamental departure from the voluntary process previously in place.

3. Conclusion

Generally speaking, government intervention under foreign investment rules is already much harder to predict than under the tried and tested merger control regimes. Our experience is that transaction timeframes are also subject to greater uncertainty, since many foreign investment regimes have very unclear and open-ended review timetables.

In addition to the relevant ministry or authority in charge of FDI screenings, specialized agencies tend to play an important role. The need for the coordinating ministry to reconcile with these stakeholders can lead to prolonged screening procedures. Moreover, procedures are (purposefully) often opaque in order to conceal the concerned national security interests. It is often unclear what the substantial issues investigated are and the authority may not share its concerns for confidentiality reasons.

Going forward, ADG companies can expect their cross-border deals to take longer to complete and they will need to consider foreign investment issues upfront to mitigate any potential delays. In addition, the various reforms and proposals will mean potentially increased scrutiny and execution risk for a broader range of deals in a number of jurisdictions. It is vital for deal teams to consider the practical considerations for managing this uncertainty and addressing individual transaction challenges upfront.

For M&A transactions in the ADG sector, we recommend considering the following action items:

1. Identify upfront those jurisdictions where buy- and sell-side M&A activity is most likely (focus jurisdictions).
2. Identify upfront those business units whose products are most likely to trigger governments' interest, e.g., aerospace and defense, energy, automotive.
3. Prepare a standard explanation of (i) your shareholder structure, corporate governance, and specifically shareholder control rights, and (ii) your business activities, particularly in sensitive areas.
4. Be transparent both in government relations and FDI screenings about the above.
5. Prepare for FDI reviews by building a network of subject matter experts internally and externally.

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11. See our in-depth client alert of the time here: https://www.hoganlovells.com/~/media/hogan-lovells/pdf/2018/2018_07_30_alert_cfius-legislation-takes-final-form.pdf?la=en.

Figure 4: Recommended process for M&A transactions

1. Clarify with M&A team the structure of the deal and the affected jurisdictions based on subsidiaries or assets
2. Identify the target activities based on information memorandum, data room, and public information
3. If not all required information is available: clarify in due diligence information required for assessment
4. High-level check based to identify possible filing requirements for deep-dive
5. In-depth assessment with local experts/local counsel
6. If FDI screenings are required: deal with impact on deal timeline an need for CPs, risk-shifting provisions, etc.

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