Retrospect: EC’s Merger Reformation of 2004 – The Value of Unofficial Pre-notification Procedure in Successful Merger Management

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Abstract

This article examines in detail the European Commission’s main instrument in aiding the fluency of merger procedures, the Best Practices on the conduct of EC merger proceedings guideline, and portrays its positive effect on the regulatory transition phase of 2004, when the new EC Merger regulation 139/2004 came into force.

Relevant background information concerning the legal context is provided in order to illustrate the anticipated hazards of the transition phase, which in retrospect never actualised. This paper seeks to answer how this scenario was avoided: What measures did the Directorate General for Competition take and as a result, what effect did this have on business communities’ freedoms and responsibilities. These conclusions are drawn from 2004’s statistical survey on European merger control.

The Blackstone/Acetex case of 2004 is provided as a case study to demonstrate the potential complications of the official merger procedure and to emphasise the importance of a well-managed pre-notification procedure preceding the actual concentration. In addition, the Commission’s increased powers to issue fines are illustrated in the form its former decisions, where the concentrating parties neglected to comply with EC competition rules.

Full Article

Introduction

The Reforms of 2004

The new EC merger regulation package, which came into force on May 1, 2004, was a long awaited reform to the problems that have been apparent in the Com-

Community merger control. The new regulation aimed to increase legal certainty of the future appraisals of mergers. More flexible time limits and the revised pre-notification procedure were expected to provide the concentrating parties more control over the actual proceedings and thus allow to track and assess the benefits that were expected to follow from the merger. This was a welcome alleviation as the new economic approach, namely the introduction of the new SIEC test on concentrations, set a new challenge for mergers with a European Community dimension.

As the procedure in itself allowed more breathing space for the concentrating parties, it came with a requirement of using complicated industrial economics models and quantitative methods of analysis. This requirement provides valuable information for the study of individual cases, but the quality of the Commission decisions comes with the cost of exponential requirement of information to be provided by the concentrating parties.

The political background for these reforms was laid down in March 2000 in Lisbon when the European leaders committed the EU to become, retrospectively quite daringly, by 2010 the most dynamic and competitive knowledge-based economy in the world capable of sustainable economic growth with more and better jobs and greater social cohesion, and respect for the environment. The Lisbon strategy was a comprehensive series of reforms. As it was claimed, actions by any one Member State would be more effective if other Member States acted in concert. In competition law, this led to the creation of the European Competition Network to bring together the National Competition Authorities, the restructured Directorate-General for Competition (“DG Comp”) and the uniform application of competition regulations.

The pressure for these reforms derived largely from the Court of First Instance’s (“CFI”) high-profile rulings on mergers where it annulled merger decisions issued by the Commission. In addition, they contained severe criticisms of both

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2 Significant Impediment to Effective Competition, see article 2, 139/2004: "A concentration which would not significantly impede effective competition in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position, shall be declared compatible with the common market.”
4 Weitbrecht (2006) I.T.L.
5 Facing the Challenge - The Lisbon strategy for growth and employment, November 2004
6 The DG Competition is a directorate under the Commission. It is responsible for establishing and implementing a coherent competition policy for the European Union.
8 Judgments of CFI, Airtours/First Choice, T-342/99 (2002), Schneider/Legrand, T-310/01.
procedural and substantive aspects of its work. The core criticism made by the CFI concerned the lack of the EC Commission’s analysis, and absence of economic evidence as it had failed to establish either a convincing justification for its decisions, either through economic analysis or through economic evidence. Due to the so-called crisis of 2002, the DG Comp was forced to accelerate the reforms. Later on, the widely debated *Impala* judgment merger demonstrated the fact that the Commission’s decisions will come under close scrutiny in the future by the European courts. As the CFI annulled the Commission’s decision to clear the concentration, it portrayed the growing importance of mutual cooperation between the merging parties and the DG Comp.

**Merger Control in EC**

*Theory behind the legislation*

The purpose of merger control is to enable competition authorities to regulate changes in market structure by deciding whether two or more commercial companies may merge, combine or consolidate their businesses into one. This includes, for example, situations when two or more previously independent undertakings merge (merger), where an undertaking acquires control of another undertaking, for example by a purchase of the stock (acquisition of control), or where a joint venture is created, performing on a lasting basis all the functions of an autonomous economic entity (full-function joint venture).

To understand the reasoning behind merger legislation, one must turn to economic theories of perfect competition and perfect monopoly. Although it does not adequately explain business behaviour in real life situations, it is still the cornerstone in legitimization of competition law. Classically, open competition is compared to what would happen in a monopolistic market. Under perfect competition, economic resources are allocated in a way that leads to the largest consumer surplus, greatest productive efficiency and dynamic stimulation of R&D processes. In contrast, monopoly leads to various inefficiencies such

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13 ECMR Art 3(2), acquisition of control described as “the possibility of exercising a decisive influence”.
as increased prices for consumers and poorer quality of goods.\textsuperscript{16} Thus, efficient merger control is elemental in preserving a market structure that is capable of providing the benefits for customers that follow from competition.

When compared to for example the US antitrust imperatives the EC competition legislation is characterized by the goal of the Single Market integration. The competition rules provide important tools for achieving the free movement of goods, services, people and capital between the Member States. Consequently, the efficiency gains reached through corporate reorganizations are the key element in improving the competitiveness of European industry as a whole.\textsuperscript{17} In this context, the right question is not whether these efficiencies should be taken into consideration but rather to how to properly take them into account.\textsuperscript{18}

EC merger control authority in Europe is divided between the EC and the EU Member States. EC’s exclusive jurisdiction is triggered when one of the two thresholds are met. Mainly these include concentrations involving enterprises with an aggregate worldwide turnover of more than Euro 5 billion and where the aggregate Community-wide turnover of each of at least two of the enterprises concerned is more than Euro 250 million will have a Community dimension\textsuperscript{19} and thus, will be investigated by the European Commission taking into account the views of Member States.\textsuperscript{20} Below this threshold, the national competition authorities of the EU Member States have the jurisdictional powers to review the merger.

The thresholds can be met even if the combined EC turnover of the concentrating parties has no link to the actual concentration, which can take place outside European Community.\textsuperscript{21} Therefore, the ECMR has an exterritorial scope even when non-European competition authorities have cleared a concentration\textsuperscript{22} although simplified procedure and waivers are open for some cases that raise no competition concerns in the EC.\textsuperscript{23} This underlines the need for expert understanding of the EC competition legislation for the global business community. Or polemically, ”The collapse of the GE-Honeywell merger shows that compa-
nies that benefit from a global market can now be governed in all they do by any of the countries or regions in which they do business.”

**DG Comp’s new approach to concentrations**

As said, to meet the challenges set out in the Lisbon Strategy, the Commission needed a new approach to merger assessments. The transition period following the adoption of a new regulatory framework was anticipated to be challenging. The staff of DG Comp, directorate in charge of competition, was already severely overloaded with work when they were expected to apply the new recast merger regulation, which came into force on 1 May 2004. Firstly, the DG Comp was increasingly expected to be able to demonstrate the economic benefits, which are expected to follow from concentrations. Therefore, the European courts had increasingly urged the DG Comp to increase economic evidence in its decisions. Secondly, the EC merger activity had been on a steady rise ranging from the year 2003’s 211 notified cases to the record-breaking year of 2006 with 356 notified cases.

From the business community’s point of view, legal certainty could also have been a downward trend. New requirements of the SIEC test and the following adoption of new complicated industrial economics models and quantitative methods of analysis combined with the long-lasting, exhaustive investigation procedure could have led to a significant increase in withdrawals, commitment decisions and outward prohibitions. However, statistical analysis of merger activity between 2004-2007 demonstrates that this, an unwanted but probable view of future did not actualise. How did the Commission manage the transition period so well? What actions did it take to meet the expectations laid down in the Lisbon strategy a few years earlier?

My hypothesis is that this can be explained largely through the adoption of the new Best Practices on Merger Proceedings guideline and especially the informal pre-notification procedure preceding the actual investigation of concentrations. This guideline, released in 2004 by the Commission, was to increase understanding of the investigation process, enhance the efficiency of investigations and to ensure a high degree of transparency and predictability of the review process, which turned out to be an effective tool in enhancing legal certainty under un-

26 See high profile CFI judgment T-342/99, Airtours v Commission.
certain times. Before viewing the pre-notification procedure in detail, it is necessary to review the whole merger process and identify the potential bottlenecks of fluent merger proceedings in light of past Commission decisions.

**Merger Proceedings Under the ECMR**

EC merger control is a front-loaded system. This means that concentrations must be notified prior to their implementation and following the conclusion of the agreement, the announcement of the public bid, or the acquisition of a controlling interest. After the notification, the concentration is suspended until the Commission either clears it or gives an outright prohibition during the so-called phase I investigation, or proceeds with extensive Phase II investigations if it raises serious doubts about its compatibility with the internal market. The latter investigation can prove to be so long-lasting, costly and exhaustive that it can lead to the abandonment of the concentration by the withdrawal of the notification.

Albeit the Commission’s decisions are subject to judicial review by the CFI, even a successful appeal may mean that due to changed market conditions, it is no longer economically feasible to proceed with the concentration. This means that it is possible to bring action in the CFI against the Commission for losses suffered, but also this judicial review by the CFI can take years.

This means that a considerable amount of information is put into the merger notification form ("Form Co"), which is often backed up by external market studies. In addition, the Commission conducts its own market studies to define the relevant markets and to assess the compatibility of the concentration with the common market. The more adequate information is provided early, the earlier it is possible to market test the concentration by the DG Comp and avoid the potential problems rising from Phase II investigations. The Commission has a strong expectance on the undertaking’s capabilities of having the resources and understanding to provide all the necessary information in the Form Co. In 2002, in the case *BP/Erdölchemie*, the Commission explicitly stated that:

"A complete Form CO with comprehensive information is of crucial importance for the Commission’s merger control procedure, inter alia due to the tight dead-

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28 ECMR, Art 4 (1).
29 Comp/M. 1663, Alcan Pechiney.
31 CFI Judgment T-212/03, Mytravel v Commission.
32 Comp/M. 2624.
lines the Commission is required to meet in these procedures, and *the notifying parties must be aware of this importance.*” (emphasis added)

Under the Phase I, the procedure can be carried out in a maximum of 35 working days. Within 15 days after notification, the EC will offer a “State of Play” meeting if it appears that the concentration raises “serious doubts” according to article 6 (1) of the ECMR. At that point, the concentrating parties will be informed about the preliminary result of the initial investigation. This leaves the notifying parties only five days to formulate possible commitments, which are due to take place within not more than 20 working days from the date of receipt of the notification. In the event of unexpected but yet significant competition, problems at this crucial moment will almost certainly lead to a Phase II investigation.

In the year 2006, there were 356 merger notifications which of 323 were found compatible according to article 6. (1) B of the ECMR and approval was obtained within 25 working days from the Commission. There has been a steady increase in the number of notified cases yet the level of withdrawals has not followed this trend, as have not Phase II investigations. Quite contrary, the level of concentrations falling under the so-called simplified procedure has risen considerably since the adoption of the new ECMR. Of the 362 decisions of the year 2006, 207 concentrations enjoyed the benefits of the simplified procedure when compared to year 2002 with 277 cases and only 103 simplified procedures. At that time, the DG Comp received heavy criticism from the CFI and was also known as the ”crisis of 2002”. These high-profile rulings led to the acceleration of the reform process. However, the pre-notification system introduced in the new Best Practices guideline, which aims to guarantee the acceptability of the Form CO through unofficial meetings and discussions before it is actually given to DG Comp, seems to have proven itself of being a valuable instrument in risk management. Before viewing the actual procedure, I will introduce the case *Blackstone/Acetex* (“Blackstone”) which portrays how the tight time schedule of the official proceedings combined with the new informational requirements set by the new ECMR can lead inevitably to costly delays in the merger procedure.

33 The first State of Play meeting will in principle take place in Phase I cases where it appears that “serious doubts” are likely to be present, and that subsequent State of Play meetings will take place during Phase II.
34 Implementing Regulation 802/2004, Art 19 (1).
36 Judgments of CFI, Airtours/First Choice, T-342/99 (2002), Schneider/Legrand, T-310/01.
38 Comp/M. 3625, Blackstone/Acetex 2004.
The Blackstone Anxiety

In the Blackstone case extensive market studies were performed during the official proceedings by both the DG Comp and the concentrating parties. Blackstone, a private equity investor, had agreed to acquire the Acetex Corporation, a maker of acetic acid. Blackstone is the owner of Celanese, a chemicals company, which is active on the same markets as Acetex. The Commission engaged in Phase II proceedings due to the serious doubts as to its compatibility with the common market and the EEA agreement as it could create significant competition concerns in horizontally overlapping markets for acetic acid, vinyl acetate monomer and acetic anhydride.

The commitments provided by the parties did not eliminate these doubts of possible unilateral and coordinated anticompetitive effects. During the case, econometric studies were undertaken both by the economists engaged by the firms and by the Chief Economist Team. After an in-depth market investigation and based on the economic evidence submitted by the parties as well as studies conducted by the CET, the case was finally declared compatible with the common market and the functioning of the EEA agreement.

Tecnor OrbiChem, a private consulting company, was responsible for providing a marketing study about the acetic acids imports into Western Europe. The data was relied on by the parties as well as the commission. LECG, a global expert economic consulting firm retained by the parties, conducted two market studies under the procedure. In addition, albeit replicating some of the studies, the Commission conducted its own statistical surveys of the concentration, in which after it cleared the concentration.

Due to the tight time limits of the post-notification schedule laid down in the ECMR, the stress will be laid on the unofficial but imperative pre-notification procedure. It is likely, that this situation could have been avoided through taking effective advantage of the new Best Practices guideline, namely the possibility of early market testing.

40 Comp/M. 3625, footnote 10.
The Benefits of the Pre-notification procedure

The Best Practices concentrates on the good conduct of pre-notification procedure, which precedes the actual investigation. In practice, it allows the concentrating parties to take full advantage of the enhanced expertise of DG Comp unofficially under strict confidence and most importantly, perform preliminary market testing without the need to perform under strict time limits. Therefore, it can be used to maximise the possibility of cleared concentration within the period of 25/35 days.

In DG Comp's experience, there is a strong causal link between the cases that have been declared incomplete and the fact that no or very little pre-notification was conducted. The time needed to successfully carry out the contacts with DG Comp varies depending on the complexity of the individual concentration. It may involve several drafts, meetings and requests of information between the notifying parties and the DG Comp team.

Even in non-problematic cases, it may take weeks or months to prepare a draft Form CO. The timetable of the pre-notification procedure sets out the framework for the negotiations. According to the Best Practices, the first contact with DG Comp should be made “as soon as possible”, since this allows it to set a specific case-team with the best expertise and facilitate its own planning of the case. Naturally, this serves the purposes of the concentrating parties also, as the case-team becomes available for consultation concurrently.

The first submission made by the concentrating parties should contain preliminary evaluations and assessments of the impact on competition in general terms. Depending on the preliminary evaluation made by the case-team the comments can be given both orally or in written form or, for more uncertain and complex cases, such as the Blackstone case, with further detailed submissions provided by the concentrating parties.

Once the concentrating parties have provided sufficient amounts of information, the DG Comp can perform early market testing and/or the notifying parties’

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42 The other areas cover the so-called state-of-play meetings during phase I and II investigations.
43 Best Practices, 3.8
44 Best Practices, 3.7.
46 Best Practices, 1.10.
position in the relevant market. The DG Comp reserves only five working days for the evaluation of a draft CO. After this, the DG Comp is ready to confirm *informally* the adequacy of the draft notification or identifies in what material respect the draft CO is incomplete. The amount of dialogue is unlimited, meaning these negotiations continue long as it will needed to draft the unsurpassed Form CO.

In addition, the pre-proceeding provides the following benefits. Firstly, the new ECMR provides, contrary to the old regulation, that the parties may formally notify the concentration in the absence of an e.g. public bid or signed contract provided that the DG Competition is satisfied, at its discretion, that the parties have demonstrated good faith intent to combine.\(^{47}\) Secondly, once an agreement is signed, the parties no longer have any time limit concerning the formal filing of the notification. Under the previous merger regulation\(^ {48}\), the parties had only seven days to file after the agreement to combine. The new rules allow the parties to have total mastery over when the concentration becomes public. As one would expect, implementation of the merger may still take place only once Commission approval has been obtained.

Lastly, the withdrawal from merger negotiations is easily achieved prior to formal notification. During phase I and II proceedings, the withdrawal from concentration can turn out to be more difficult as the Commission can adopt a prohibition or publish even a detailed press release\(^ {49}\) “unless the undertakings concerned have demonstrated to the satisfaction of the Commission that they have abandoned the concentration.” As a general principle, the requirements for the proof of the abandonment must correspond to the initial act that was considered sufficient to make the concentration notifiable; the *status quo ante* has to be shown.\(^ {51}\) Therefore, the Best Practices provides companies an opportunity to perform *ex ante* evaluation and impact assessment and thus limit, for example, the potential adverse media coverage following from publicity of the official proceeding. As we have seen now, the new regulation package allows more power and breathing space for the concentrating parties, but this freedom comes with a price. Under the new ECMR, non-compliance is now enforced with tougher fines for non-compliance.

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\(^{47}\) 139/2004 article 6 (1).
\(^{48}\) 4064/89.
\(^{49}\) Case Alcan/Pechiney, Commission Press Release IP/00/258, 14 March 2000.
\(^{50}\) 139/2004 article 6 (1c).
\(^{51}\) DG Competition Information note on abandonment of concentrations.
The Commission’s toughened attitude towards non-compliance

The Commissions powers to issue fines were substantially increased under the new ECMR. As one would expect, even an extensive pre-notification procedure does not guarantee a clearance under the Phase I investigation, if the Form Co is incomplete, incorrect or misleading. Even more, if the Community thresholds are exceeded and a community dimension is created, the Commission has a strong expectance on such an undertaking’s capacity to comply with all its demands.

Under the old merger regulation 4064/1989 the Commission could only give fines from EUR 1000 to 50 000 where the concentrating party supplied incorrect or misleading information in its Form Co. Under the new ECMR 14 (1), fines may be imposed up to one per cent of the worldwide aggregate turnover of the undertaking.

In the case A.P. Møller52, the Commission took into account the size of the company concerned, its global activities and the former experience in competition law when it assessed the capabilities of the company to acknowledge the need for notification. A.P. Møller was eventually fined for both not notifying the concentration in one week after the completion (14(A)1) of the concentration and putting it to effect prior to notification (14(2)B) for a total of EUR 219 000. The Commission has now the power under Article 14(2) (a) of the ECMR to impose fines up to 10 per cent of the aggregate turnover of the undertakings concerned, on a party that, intentionally or negligently, fails to notify a concentration - not just for proceeding without notifying as under the old regulation.

Moreover, the Commission is now entitled to impose periodic penalty payments for undertakings that fail to supply information by decision. This includes also third parties, which illustrates the Commission’s wide powers to obtain relevant information during the official proceedings.53

Where the Commission requires an undertaking to supply information by decision, it will specify what information is required and under what time limit.54 Infringements can now lead to periodic penalty payments up to five per cent of the average daily aggregate turnover of the undertaking. In the case Mitsubishi Heavy

52 Comp/M. 969.
53 139/2004, article 11.(1).
54 139/2004, article 11 (3).
In the year 1999, the Commission imposed fines of EUR 900,000 to a reluctant third party for having supplied incomplete information to the Commission under the merger proceedings. At the time the Commission was entitled to impose fines not exceeding EUR 25,000 for each day of delay calculated from the date set in its decision.

Pre-notification procedure is open also for such third parties that might be liable to supply information under the official proceedings. Under the previous regulation, third parties did not seem to have sufficient interest in providing relevant information on a timely basis. Under the new tougher legislation, this might not be the case. Presumably, third parties holding such relevant information might have found there an incentive to cooperate already during the unofficial procedure and thus contribute to a comprehensive Form CO and fluent merger procedure.

Conclusions

The immediate effect of the 2004 merger reforms was likely to lead to increased uncertainty for the concentrating parties. The adoption of the new market test combined with competition authorities’ strong expectancy on companies’ capabilities to adopt and implement the new legislation accordingly could have potentially led to a substantial increase in withdrawals, commitment decisions and outward prohibitions. This would have had a negative effect on the whole European industry and thus, its competitiveness on the global level. This development would have been the total opposite of what the reforms were originally intended to have an effect on. With the effective combination of the enhanced expertise of the DG Comp and the pre-notification procedure, these obstacles were avoided before their actualisation.

The CCE’s new economic expertise provides fluent co-operation through consulting already at the earliest steps of the merger negotiations. A well-implemented strategy is an essential element in ensuring a clearance decision by the Commission at the earliest point possible. The value of early negotiations is that pre-emptive meetings can cut down the regulatory scrutiny of 110 days to less than one month under the Phase I or simplified proceedings. The business community holds now more freedoms in merger procedure, but that comes with the price of significantly more severe consequences for non-compliance.

55 Comp/M. 1634.

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