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The Scope of Application of the Merger Control Regulation

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Abstract

This Article attempts to provide a practical guide to individuals attempting to determine which mergers and acquisitions fall under Community jurisdiction. Part I reviews the basic considerations the European Economic Community Regulation No. 4064/89 gives to the term "Community dimension." Part II examines the separation of jurisdiction between the Commission of the European Communities and the Member States in light of these two propositions.

ARTICLES

THE SCOPE OF APPLICATION OF THE MERGER CONTROL REGULATION†

Christopher Jones *

INTRODUCTION

Three central themes run through the European Economic Community Regulation No. 4064/89 (the "Merger Control Regulation" or the "Regulation"):[1] control according to competition based criteria, pre-merger notification, and the application of a single regulatory control to any particular operation. In order that the third of these principles is respected, the Regulation defines a "concentration with a Community dimension" such that all such concentrations fall within the jurisdiction of the Commission of the European Communities (the "Commission"); those without a Community dimension do not. Although there are exceptions to this basic distinction, these exceptions are of limited importance and are based on solid economic reasoning. If intelligently applied by the relevant authorities and institutions, they will not result in the exercise of more than one remedy to any given concentration within the Community.

The Regulation applies only to concentrations, and not to structures by which independent undertakings coordinate their commercial activities. This distinction, which is set out in the Regulation itself and explained by a Commission notice, is valid, and takes account of the structure of the competition rules in the Treaty Establishing the European Economic Community (the "EEC Treaty").[2] The distinction between the two

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* Official, Commission of the European Communities. All views expressed are strictly personal to the Author.

1. O.J. L 395/1 (1989), Common Mkt. Rep. (CCH) ¶ 2839, corrected version in O.J. L 257/13 (1990) [hereinafter Merger Control Regulation].

2. *See* Treaty Establishing the European Economic Community, Mar. 25, 1957, arts. 85-86, 1973 Gr. Brit. T.S. No. 1 (Cmd. 5179-II), 298 U.N.T.S. 3 (1958) [hereinafter EEC Treaty].

concepts makes economic and legal sense, and it is not difficult to apply in practice.

This Article seeks to provide a practical guide to individuals attempting to determine which mergers and acquisitions fall under Community jurisdiction. Part I reviews the basic considerations the Regulation gives to the term "Community dimension." Part II examines the separation of jurisdiction between the Commission and the Member States in light of these two propositions.

I. *CONCENTRATIONS WITH A COMMUNITY DIMENSION*

A. *Community Dimension*

1. Basic Considerations

The effects of mergers and acquisitions should be the concern of the respective country alone if the effects are limited to that sole Member State. Irrespective of considerations as to the proper limits of the secession of sovereignty to supra-national institutions, a national authority will be better placed to determine the impact of such operations on local markets and will thus be better able to reach correct regulatory conclusions. Concentrations which stretch throughout a number of Member States may be more appropriately dealt with by the Commission, which is in a better position to view the impact of the operation Community-wide. How is this distinction given effect?

Many solutions can be envisaged that involve market share tests in differing geographic areas and cross-border trade considerations. Although these solutions have the merit of accurately reflecting this theoretical division, they are difficult to apply. Nevertheless, many such tests were put forward throughout the sixteen years of negotiation and redraft that led to the adoption of the Regulation. During the final series of negotiations, however, emphasis was placed on the need for a test that is easily applied. The Council of Ministers of the European Communities (the "Council") therefore adopted a three-stage test based on the size of the parties and the geographic split of their activities. Thus, article 1(2) of the Regulation states that

> [f]or the purposes of this Regulation, a concentration has a

> community dimension where: (a) the aggregate worldwide turnover of each of at least two of the undertakings concerned is more than ECU 5,000 million, and (b) the aggregate Community-wide turnover of each of at least two of the undertakings concerned is more than ECU 250 million, unless each of the undertakings concerned achieves more than two-thirds of its aggregate Community-wide turnover within one and the same Member State.[3]

The size-related test is based upon the fiction that mergers and acquisitions by and between large companies are likely to have a Community-wide effect. Although this is not necessarily true, it will be correct in the majority of cases, particularly as the 1992 process results in successful companies expanding from national to pan-European markets.

Complementing this is the "geographic split of turnover" test, which enables Member States to retain jurisdiction over large concentrations, the effects of which are nevertheless largely confined to that Member State.

The ECU 250 million provision has a dual purpose. First, it provides a *de minimis*, excluding operations involving companies or assets of insufficient importance to trigger Community jurisdiction. Secondly, it acts to determine the extraterritorial scope of application of the Regulation. By this test, the Community apparently claims jurisdiction over operations which have significant effects in the Community:[4] any concentration between two undertakings situated outside the Community which meet the ECU 5 billion test and which have ECU 250 million turnover in the Community will, subject to the two-thirds rule, require notification.[5]

The thresholds set for the size-related tests are very high. As a result, they fail to reflect accurately the theoretically correct division of responsibilities between the Community and the Member States. Many concentrations falling below the thresholds will be concluded with the single market process in

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3. Merger Control Regulation, *supra* note 1, art. 1(2), O.J. L 257/13, at 16.

4. This raises interesting problems in determining the compatibility of this test with that of "implementation within the Community" as set out by the Court in the *Woodpulp* judgement. Woodpulp, O.J. L 85/1 (1985), Common Mkt. Rep. (CCH) ¶ 10,654.

5. It is submitted that as a consequence of this, a considerable number of mergers and acquisitions centered outside the EEC will fall under Community jurisdiction, for example, the Sony purchase of Columbia Pictures.

mind and will have pan-European competitive consequences. It should be remembered, however, that the thresholds will be reviewed by the Council by the end of 1993 at the latest. It is hoped that on that occasion the thresholds will be lowered to enable the theory to become at least closer to reality.

Commission estimates indicate that approximately eighty notifications per year may be expected. This figure has been steadily rising over the previous four years and is expected to continue increasing with the progress of the 1992 process. The use of a simple test may upset the purists but will delight the lawyers, administrators, and businessmen, who agree that the need for clarity and simplicity outweighs the need for adherence to the theoretical considerations of separation of jurisdiction.

2. Calculation of Turnover

a. Basic Principles

Article 5(1) of the Regulation describes how "turnover" is to be defined for the purposes of a Community dimension.[6] Aggregate turnover is deemed to include "the amounts derived by the undertakings concerned in the preceding financial year from the sale of products and the provision of services falling within the undertakings' ordinary activities after deduction of sales rebates and of value added tax and other taxes directly related to turnover,"[7] with intra-group sales being excluded.

- The use of the preceding financial year's figures is necessary; otherwise specific amounts would need to be prepared for each notifiable concentration. Although the occurrence of a substantial acquisition or divestiture since the closure of the preceding financial year may result in a somewhat artificial picture of the merging companies being presented, this is inevitable. It is also not problematic when the aim of the thresholds are kept in mind.
- The exclusion of VAT and other taxes directly related to turnover concerns, inter alia, excise duties.
- Pursuant to article 5(4) the turnover of the entire group

6. Merger Control Regulation, *supra* note 1, art. 5(1), O.J. L 257/13, at 18.
7. *Id.*

> to which the undertakings concerned belong must be included in the calculation. The meaning of group in this context is defined in that article, when read in the light of the definition of "control" in article 3.[8]

b. Exceptions to the Basic Principle

i. Acquisition of Parts

Where one undertaking acquires part of another, and irrespective of whether that part concerns only assets or a whole company, only the turnover of the acquiring group and that attributable to the acquired part is considered.[9] This exception simply reflects the aim of the turnover test to ascertain the economic importance of the undertakings concerned. Additionally, in order to prevent "salami tactics" or creeping acquisitions, an operation undertaken by the same group within two years of a similar approach as the original operation results in the two operations being combined.

ii. Joint Ventures

If an undertaking is jointly controlled with a non-group member, only the proportion of the joint venture's turnover equivalent to the number of undertakings controlling the joint venture is considered.[10] Sales by the joint venture to the group are excluded from the calculation.

iii. Concentrative Joint Ventures

If two undertakings transfer all their activities in one product market to a joint undertaking and one or both of them withdraws entirely from that market, this may constitute a concentration within the meaning of the Regulation. In such cases, should the turnover of the assets transferred alone be taken into account, or those of the parent and holding companies as well? Article 5(2) provides no definitive answer.[11] It is submitted that the turnover of both groups (including that of the joint venture split amongst the groups) be included in the

8. *See id.* art. 5(4), O.J. L 257/13, at 18.
9. *Id.* art. 5(2), O.J. L 257/13, at 18.
10. *Id.* art. 5(4), O.J. L 257/13, at 18.
11. *See id.* art. 5(2), O.J. L 257/13, at 18.

calculation. The test aims to determine the economic importance of parties to the transaction. Because the parents will have a role to play in the joint venture's future behavior, they should therefore be included.

iv. Special Rules for Credit Institutions and Insurance Undertakings

An asset-based test replaces the turnover test in the case of credit institutions.[12] The value of premiums is used for insurance undertakings.[13]

B. *Concentration*

1. Basic Principles

The Regulation defines a concentration on the basis of the existence of a change of control in the whole or part of an undertaking or undertakings.[14] It follows from this definition and that of the term "control" that the Commission examines each concentration on a case-by-case basis to determine, as a matter of fact, whether control has passed. The method by which control is acquired is irrelevant; for example, it may be by acquisition of shares, voting rights, the control of assets, seats on the board of directors, or contract. This definition is a very practical one and will raise no difficulties in ninety-nine percent of the concentrations.

2. Exceptions to the Basic Principle

Article 3(5) provides that a concentration shall not be deemed to arise where credit or financial institutions acquire securities on a temporary basis with a view to reselling them, and voting rights are not used to determine the competitive behavior of the undertaking in question.[15] Voting rights may be used with a view to preparing the sale of all or part of the undertaking's securities only if the sale takes place within one year of the acquisition of the securities, subject to an express agreement by the Commission granting an extension to this

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12. *Id.* art. 5(3), O.J. L 257/13, at 18.
13. *Id.*
14. *Id.* arts. 3(1), (3) & (4), O.J. L 257/13, at 17.
15. *Id.* art. 3(5), O.J. L 257/13, at 17.

period.[16] Furthermore, article 3(5) in certain circumstances permits financial holding companies to acquire securities for investment purposes but to exercise voting rights only to maintain the full value of the investment and not to determine the competitive conduct of the undertakings in question.[17]

3. The Distinction Between Co-Ordination and Concentrations: Partial Mergers

a. Introduction

If a cartel-type agreement exists between undertakings occupying thirty percent of a relevant market, antitrust authorities are unlikely to regard the resultant restriction on competition as unimportant. If undertakings with a thirty percent relevant market share between them merge, thus eliminating competition between them, the operation is likely to be cleared.

Concentrations resulting in permanent structural market change are considered to produce benefits not resulting from commercial cooperation between independent firms, justifying this differing treatment.[18] It is necessary to develop a method or test to determine which set of rules—merger or cartel—applies to any given operation.[19] For most operations, this is a simple task: cartels have none of the characteristics of permanent structural change typical of mergers, and mergers and acquisitions between previously independent firms display few of the characteristics of cartels.[20]

This distinction is less evident for other types of operations, in particular joint ventures. A joint venture can be a cartel: two companies active in the same market set up a joint

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16. *Id.*

17. *Id.* Article 3(5) also provides that a person acquires control when he is responsible for the winding-up or liquidation of an undertaking. *Id.*

18. *See* Götting & Nikowitz, *EEC Merger Control*, 13 FORDHAM INT'L L.J. 185 (1989-1990) (distinguishing concentrative joint ventures from cooperative joint ventures).

19. This is true at least under the Community's antitrust rules. The possibility of different institutions applying the same rules with respect to the same operation, and of the differing remedies available with respect to the differing rules, renders the simultaneous application of Articles 85 and 86 or the Merger Control Regulation at best inadvisable.

20. In the event they do possess the same characteristics, those cartel elements are usually disassociable from the merger and can be dealt with separately.

sales agency which fixes the prices of its parents at identical levels. A joint venture can also be a pure merger: two companies devote their entire resources in one market, where their cooperation in this sector has no effect on the product markets in which they remain active.

The Commission has always taken the view that in order to benefit from the more liberal provision, an operation should fulfill two criteria: (1) it should result in a change on the market of the nature likely to bring the perceived benefits of concentrations, and (2) it should not have the result of restricting the free market mechanism. It should therefore result in a long-term or permanent structural change on the market and should not, directly or indirectly, affect the competitive relationship between the parties.

Prior to the entry into force of the Merger Control Regulation, the Commission applied a partial merger theory to determine which joint ventures were mergers (to be scrutinized under Article 86 of the EEC Treaty) and which were cooperations between independent companies (falling under Article 85 of the EEC Treaty). It appears that the Commission would consider a joint venture to be a partial merger[21] if two companies created a jointly owned subsidiary and (1) both (or perhaps only one) of the parents completely and irreversibly withdrew from the markets in which the joint venture was active, and (2) the markets in which the joint venture was active were sufficiently remote from those on which the parents remained to ensure that no anti-competitive spill-over effect occurs on the parent's conduct due to their cooperation in the joint venture's market.[22]

This test has the disadvantage of being difficult to apply, because the determination of whether or not a company has completely and irreversibly withdrawn from a market requires an estimate of the extent to which the parents are actual or potential competitors of the joint venture. It is nevertheless logical. The first part of the test determines the concentrative

21. *See, e.g.*, SHV/Chevron, Commission Decision of Dec. 20, 1974, O.J. L 38/14 (1975); De Laval/Stork, Commission Decision of July 25, 1977, O.J. L 215, at ¶ 5 (1977); ENI/Montedison, Commission Decision of Dec. 4, 1986, O.J. L 5/13 (1987). *See* Banks, *Mergers and Partial Mergers under EEC Law*, in 1987 FORDHAM CORP. L. INST. 373 (B. Hawk ed. 1988).

22. *See* COMM'N, SIXTH REPORT ON COMPETITION POLICY ¶ 178 (1976).

nature of the operation and the permanent nature of the structural change. The second ensures that any spill-over effects are not sufficiently large to require the operation to be examined under the cartel rules. It is also a strict test, motivated by the Commission's desire that hidden "cartel type" joint ventures do not escape the more severe Article 85.

Article 3(2) of the Regulation provides the following test:

> An operation, including the creation of a joint venture, which has as its object or effect the coordination of the competitive behaviour of undertakings which remain independent shall not constitute a concentration.... The creation of a joint venture performing on a lasting basis all the functions of an autonomous economic entity, which does not give rise to co-ordination of the competitive behavior of the parties amongst themselves or between them and the joint venture, shall constitute a concentration within the meaning of [the Regulation].[23]

In order to be qualified as a concentration, a joint venture must therefore fulfill a positive condition (performing on a lasting basis all the functions of an autonomous economic entity) and a negative condition (not giving rise to the coordination of competitive conduct). Just when you thought it was safe to go into the office the test changed, or has it? Under the partial merger theory, there was no obligation to prove that the joint venture could perform on a lasting basis all the functions of an autonomous economic entity. This is a puzzling addition, but it appears that it can be explained if one assumes that the autonomous economic entity test is simply an expression of the requirement that a real structural change on the market must occur. If a joint venture is created which is not a separate economic entity from its parents, it is unlikely that the requisite structural change has occurred. It might be argued that the adoption of this test is too narrow and does not enable the Commission to examine, on a case-by-case basis, whether or not a permanent structural change has in fact taken place. However, the two concepts are in fact very similar. If a joint venture is an autonomous economic entity, it will undoubtedly be the result of permanent structural change. If applied in an appropriate manner by the Commission, the change in word-

23. Merger Control Regulation, *supra* note 1, art. 3(2), O.J. L 257/13, at 17.

ing is unlikely to result in any appreciable change from the "partial merger" test followed under Article 86, and will continue to follow the economic basis behind the distinction. Furthermore, the wording chosen is more readily understandable by the business community which, in this Author's experience, is less interested in the finer points of legal analysis than the legal profession.

The second part of the test, "coordination of the competitive behaviour of the parties amongst themselves or between them and the joint venture,"[24] is more readily understandable. If the creation of a joint venture produces a permanent structural market change, but nonetheless either serves as a vehicle for the coordination of the market behavior of the undertakings or has appreciable spill-over effects on their operations outside of the joint venture, it should be examined under the cartel provisions, not the merger ones.

The establishment of a joint venture can have the direct or indirect effect of coordinating the competitive behavior of the parents.[25] If two parents set up a joint venture operating on a relevant market on which they remain active, this is likely to have a direct effect on the competitive relationship between them irrespective of the degree of independence of the joint venture. If two parents active in the food retailing business set up a joint venture company to bake bread, this will have an indirect or "spill-over" effect on the parents' retailing activities.

b. The Notice

On August 14, 1990, the Commission published a notice (the "Notice") designed "to define as clearly as possible, in the interests of legal certainty, concentrative and cooperative situations."[26] This Notice (1) defines the concept of a joint venture, (2) examines the requirement that the joint venture performs on a lasting basis all the functions of an autonomous economic entity, (3) examines the requirement that the opera-

24. *Id.*

25. A checklist for determining this in individual cases is set out in COMM'N, THIRTEENTH REPORT ON COMPETITION POLICY ¶ 55 (1984).

26. O.J. C 203/10 (1990) [hereinafter Notice].

tion creates no coordination of competitive behavior, and (4) gives four examples.

1. *The Concept of a Joint Venture*

To be a joint venture, the undertaking in question must be jointly controlled. If it is not, the operation may be a simple acquisition by the controlling company. If, for example, Company A sells securities in a subsidiary to Company B but that sale is insufficient to establish joint control, the agreement must be examined pursuant to Articles 85 and/or 86.[27] Joint control is said to exist where the parent companies agree on decisions concerning the joint venture's activities. The particular method from which joint control is derived, whether achieved by shares, voting rights, or contract, is irrelevant. The Notice states that "[t]here is no joint control where one of the parent companies can decide alone on the joint venture's commercial activities."[28]

2. *Positive Condition: Joint Venture Performing on a Lasting Basis All the Functions of an Autonomous Economic Entity*

According to the Notice the joint venture must, in order to fulfill the above-referenced requirement, meet three criteria:

> (1) Act as an independent supplier and buyer on the market. As a consequence the joint venture will not be, at least in the medium/long term, substantially dependent on its parents for the maintenance and development of its business.
> (2) Have the human and material resources to continue in business independently of its parent companies in the long run.
> (3) Be in a position to exercise its own commercial policy. This does not mean that the parent companies should not retain the right to control certain aspects of the company in order to maintain the value of their investment (*e.g.*, concerning "alterations of the objects of the company, increases or reductions of capital, or the application of prof-

27. *See id.* ¶¶ 14 & 15, O.J. C 203/10, at 11; British American Tobacco Co. v. Commission, Joined Cases 142 & 156/84, 1987 E.C.R. 4487, Common Mkt. Rep. (CCH) ¶ 14,405.

28. Notice, *supra* note 26, ¶ 12, O.J. C 203/10, at 11.

its").[29]

Thus, it appears that the requirement that the joint venture must perform on a lasting basis all the functions of an autonomous economic entity has itself been strictly interpreted. If the Commission had explicitly interpreted this phrase as an indication of the fact that a permanent structural change must result, it would be more easily understandable. The existence of a real company with assets, not a simple shell, is therefore necessary. The phrase in the Merger Control Regulation gives the Commission considerable leeway in determining, on a case-by-case basis, whether such a structure exists. However, the requirement that the joint venture exercise its own commercial policy goes much further than this. If, for example, both parents have completely and irrevocably withdrawn from the joint venture's market, and the joint venture itself is a permanent structure, it is difficult to see why the economic benefits presumed to mergers would not flow to the joint venture simply because it received marketing instructions or advice from one or both of its parents. The argument that the parents would in fact be coordinating their behavior in that market is irrelevant, if there are no spill-over effects on their other operations; such cooperation is the very essence of a concentration.

The test in the Regulation has thus a certain logic and economic justification, and in the interpretation given to it by the Commission should be understood in this light. It is therefore submitted that in each case the Commission must determine whether an autonomous economic entity (or permanent structural change) exists. In doing so, it must take account of the factors outlined in the Notice. The factors are indicative, not determinative.

3. *Negative Condition: Absence of Coordination of Competitive Behavior*

Irrespective of the structure of the operation, the central test under the partial merger theory and the Merger Control Regulation centers on the competitive relationship between the parents and the joint venture.[30] If, for example, two tooth-

29. *Id.* ¶ 19, O.J. C 203/10, at 12.
30. Merger Control Regulation, *supra* note 1, art. 3(2), O.J. L 257/13, at 17.

paste manufacturers set up a joint venture and combine their research and development and sales operations, irrespective of any economic independence of action of that joint venture, that collaboration will have a cartel-like effect on the parents' toothpaste production business. Such an operation should therefore be examined under the cartel provisions and not the concentration provisions. If, on the other hand, a steel company and a manufacturer of video-recorders cede their entire toothpaste business to a joint venture, that is unlikely to affect their remaining operations and may be examined as a concentration.[31]

This distinction is explained as follows by the Notice:

> There must not be such coordination either between the parent companies themselves or between any or all of them on the one hand and the joint venture on the other hand. Such coordination must not be an object of the establishment or operation of the joint venture, nor may it be the consequence thereof. The joint venture is not to be regarded as concentrative if as a result of the agreement to set up the joint venture or as a result of its existence or activities it is reasonably foreseeable that the competitive behavior of a parent of the joint venture on the relevant market will be influenced. Conversely, *there will normally be no foreseeable coordination when all the parent companies withdraw entirely and permanently from the joint venture's market and do not operate on markets neighbouring those of the joint venture's.*[32]

This definition is entirely logical. If there is neither a direct effect on the competitive relationship of the parents nor any spill-over between the joint venture's activities and those of the parents, there is no risk that the concentration will result in a restriction of competition between the parents in their remaining activities.

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31. This example illustrates the difficulty that one would have in understanding the "independent economic entity" test were it to be interpreted as anything save a manifestation of the need for permanent structural change. In cases in which "spill-over" effects are unlikely, it is normal (but not inevitable) that the resultant company will be an entire production unit containing all the upstream and downstream operations of its parents in the sector in question. It is in this light that any other interpretation of the autonomy test would reflect not some deeply held conviction that the economic benefits available to concentrations flow to *wholly* independent units alone, but a confusion in the role played by independence of the joint venture in determining spill-over effects.

32. Notice, *supra* note 26, ¶ 20, O.J. C 203/10, at 12 (emphasis added).

The Notice then continues in paragraph 22 to state that:

> In other cases, [those in which the parents are active in the markets of the joint venture or in neighboring or upstream or downstream markets] the risk of coordination will be relatively small where the parents limit the influence they exercise to the joint venture's strategic decisions, such as those concerning the future direction of investment, and when they express their financial, rather than their market-oriented, interests.[33]

This paragraph appears to indicate that even if there is a potential spill-over effect due to the proximity of markets in which the joint venture and its parents operate, a joint venture may be considered a concentration if *as a matter of fact* it can act as an independent competitor of its parents, thus reducing or eliminating any possible spill-over effects. This is welcomed because it gives a strong indication that the Commission will examine each case to determine the competitive relationship between the parents and the joint venture on the basis of the facts of each case.[34] This indication is strengthened by the wording of paragraph 23, which states that the "decisive factor is not the legal form of the relationship between the parent companies and between them and the [joint venture]. The direct or indirect, actual or potential effects of the establishment and operation of the [joint venture] on market relationships, have determinant importance."[35]

4. *Examples*

i. Joint Ventures That Take Over Pre-Existing Activities of Parent Companies

If all the parent companies transfer all of their assets and withdraw from any given relevant product and geographic market, and the nature of the parents' remaining activities produce no likelihood of spill-over effects in both product and geographic terms, the operation is likely to be concentrative.

33. *Id.* ¶ 22, O.J. C 203/10, at 12.

34. It also again highlights the difficulty of the first "independence" test. A joint venture fails the first test if it is not independent from its parents in its marketing policy. Its independence for the purpose of establishing, as a matter of fact, whether or not the operation will have spill-over effects loses much, if not all, of its significance.

35. Notice, *supra* note 26, ¶ 23, O.J. C 203/10, at 12.

To determine whether or not the parents have withdrawn permanently, the Commission will examine whether they are actual or potential competitors of the joint venture. The Notice states at paragraph 25 that the following principles will apply: "the notion of potential competition is to be interpreted realistically . . . [the possibility to enter a market must] be a realistic option and represent a commercially reasonable course in the light of all objective circumstances."[36]

If parents continue to compete in the joint venture's product markets but operate only in geographic areas outside the sphere of influence of the joint venture, the Commission will examine the degree of difficulty that either party would have in extending their activities. As barriers to entry are ever decreasing in the Community, it will be increasingly difficult to convince the Commission that entry into one part of the common market from another is not a realistic possibility.

ii. Joint Ventures that Enter the Parents' Market

Paragraph 33 of the Notice states that

> [w]here the parent companies, or one of them, remain active on the joint venture's market or remain potential competitors of the joint venture, a coordination of competitive behavior between the parent companies or between them and the joint venture must be presumed. So long as this presumption is not rebutted, the Commission will take it that the establishment of the joint venture does not fall under article 3(2), subparagraph 2 of the Regulation.[37]

If both parent companies operate in the joint venture's market, then it is highly likely that the operation of the joint venture will directly affect the competitive relationship between the parents. Equally, if only one parent remains fully active on the joint venture's market, a coordination of competitive conduct may result insofar as the withdrawing parent retains strategic interests in the joint venture's operations. The suspicion will be that one party has in fact ceded its interests to the joint venture, but by the retention of its interest in the joint venture's activities is in fact coordinating its competitive conduct in that market with that of the other parent.

36. *Id.* ¶ 25, O.J. C 203/10, at 13.
37. *Id.* ¶ 33, O.J. C 203/10, at 14.

It is thus submitted that the negative presumption is an expression of the difficulty that companies will face in convincing the Commission that one of them has, as a matter of fact, withdrawn from the joint venture's market and does not represent a potential competitor, and that the joint venture's operation will not have anti-competitive spill-over effects on the withdrawing parents' other activities. The withdrawing parent may, for example, retain activities that use similar technical or marketing skills to those of the joint venture.

When one of the parents becomes a holding company, exercising its share of the control over the joint venture only to maximize the value of its investment, or a conglomerate disposes of an activity remote from its other main-stream activities, it should be possible to convince the Commission that despite the presence of one parent company in the joint venture's market, a concentration occurs. In the case of an industrial company where only one of a number of associated product lines or sectors are devoted to the joint venture, this argument will be far more difficult to prove.

iii. Joint Ventures that Undertake New Activities on Behalf of the Parent Companies

If a new market entered by the joint venture is one that the parents would be unable or unlikely to enter alone, and that market is sufficiently remote from the parents in geographic or product terms to present a risk of spill-over effects, the joint venture is likely to be concentrative.

iv. Joint Ventures that Operate in Upstream, Downstream, or Neighboring Markets

The Commission will examine whether, as a matter of fact, the joint venture's operation will have an anti-competitive effect on the competitive relationship between the parents.

4. Conclusion

The concentration-cooperation distinction contained in article 3 of the Regulation[38] has only one aim: to determine whether the more severe prohibition test of Article 85 of the

38. Merger Control Regulation, *supra* note 1, art. 3, O.J. L 257/13, at 17.

EEC Treaty or the more liberal dominant position test of the Merger Control Regulation applies to any operation.

The success of the test in the Regulation, when read together with the Notice, should be judged according to two criteria:

(1) Does the chosen method of distinction reflect economic reality?

(2) Is the chosen method easy to apply?

This analysis indicates that the ideal test for the purpose of ensuring that economic theory is reflected in the application of the concentration-cooperation distinction would be simply to examine, on a case-by-case basis, (1) the effect of the operation on the competitive relationship between the parents of the joint venture, and (2) whether or not a permanent structural change results. If the activities of the joint venture would be likely to affect the competitive relationship between the parents either on identical, neighboring, upstream or downstream geographic, or product markets, the operation should be examined under the Article 85 "cartel provision." If it has no such effects, it would be appropriate to examine the operation under the Merger Control Regulation. The adoption of such a flexible case-by-case test, however, makes it very difficult for undertakings to determine in advance under which set of rules they will fall. The Regulation thus contains a more specific two-stage test.

The two-stage test in the Regulation largely reflects the economic background. At first sight, however, the first part of this test, the autonomous economic entity, appears to be interpreted in the Notice in a manner difficult to justify on economic grounds. Insofar as this would result in concentrations which should be considered under the Merger Control Regulation failing under Article 85(1), the jurisdictional test would become substantive. If this analysis is correct, this would be of concern as it would result in operations producing economic benefits not available to cartels being considered—and possibly prohibited—under Article 85(1). The factors listed in the Notice should therefore be considered as relevant but not necessarily determinative.

For ease of application and clarity, a simple numerical test similar to that defining the thresholds for the existence of a

Community dimension but relating to the acquisition of assets or shares is attractive. Such a simple test would, however, fail to reflect the economic basis behind the need for the distinction.

Although any test that reflects the economic background will create difficulties in many cases at least until a substantial body of precedent is built up, the Regulation and Notice do give fairly clear guidelines. It has been argued elsewhere that the Notice will have the effect of increasing uncertainty and thus raising transaction costs. It is submitted that this is not true. Irrespective of any doubts as to the extent to which the Notice reflects economic reality, it sets out clearly which operations will and which will not be considered concentrations. In such circumstances they are likely to decrease, not raise, transaction costs.

II. *SEPARATION OF JURISDICTION BETWEEN THE COMMISSION AND ITS MEMBER STATES*

A. *Basic Principle*

The Merger Control Regulation provides that the Regulation alone applies to concentrations with a Community dimension,[39] and that the Commission has exclusive competence, subject to review by the Court of Justice of the European Communities (the "Court of Justice" or the "Court"), to adopt the decisions provided for in the Regulation.[40] The Regulation furthermore mandates that Member States shall not apply their national legislation on competition to concentrations with a Community dimension,[41] and that Council regulations implementing Articles 85 and 86 are inapplicable to concentrations with or without a Community dimension.[42] Thus, subject to the exceptions set out below, the Commission alone has competence to examine concentrations with a Community dimension under its competition rules, and the Member States have the exclusive competence to examine concentrations without a Community dimension.

39. *Id.* art. 22(1), O.J. L 257/13, at 24.
40. *Id.*
41. *Id.* art. 21(2), O.J. L 257/13, at 24.
42. *Id.* art. 22(2), O.J. L 257/13, at 24.

B. *First Exception: Referral of a Concentration to a Member State*

Member States receive a copy of all notifications. They may also carry out initial inquiries into the operation. According to the Regulation, if a Member State concludes that the "concentration threatens to create or to strengthen a dominant position as a result of which effective competition would be significantly impeded on a market, within that Member State, which presents all the characteristics of a distinct market, be it a substantial part of the common market or not," it may request the Commission to refer that concentration to the competent authority of that Member State.[43]

The Commission may pursue one of several courses of action in reply to a request for referral:[44] (1) it may concur that a distinct market and threat to competition exists, and decide to deal with the case itself to restore effective competition on the market in question, thus opening proceedings; or (2) it may concur that a distinct market and threat to competition exists, and decide that the Member State is in a better position to deal with the problem than the Commission. In the latter scenario, the Commission would refer the case back to the Member State, or (3) it may disagree that a distinct market and/or threat to competition exists, and adopt a decision refusing to refer the concentration back and approve the operation.[45] It is submitted that the existence of such a provision in the Regulation is to be welcomed.

A concentration with a Community dimension will, in certain cases, give rise to purely local problems. An example of this might be a concentration between two conglomerates that both have interests in the provision of bus services within a particular region of one Member State. Such a problem can be more appropriately dealt with by a national authority with resources better adapted to examining local rather than national or multi-national markets. Indeed, a Member State would be more likely to identify such localized problems than the Commission in the first place. The mechanism enabling referral

43. *See id.* art. 9(1) & 9(3), O.J. L 257/13, at 20. Article 9(7) explains how the geographical reference market is to be defined by drawing heavily on judgments of the Court of Justice of the European Communities defining the relevant geographic market under Article 86. *Id.* art. 9(7), O.J. L 257/13, at 20.

44. *Id.* art. 9(3), O.J. L 257/13, at 20.

45. *Id.*

will permit a flexible and appropriate system of control in any given case, and makes perfect economic and procedural sense.

The main disadvantage of this provision is that in theory it represents a partial breach of the underlying principle in the Regulation, that any given operation is subject to only one system of control. If used intelligently by both Member States and the Commission, however, the breach will be innocuous. The reasons for this are:

> (1) Article 19(2) of the Regulation requires that the Commission carry out the procedures set out in the Regulation in "close and constant liaison" with the competent authorities of the Member States.[46] As a consequence of this, if a Member State identifies a threat to competition on a market of Community significance, it may inform the Commission of this fact at an early stage. The Commission may then take the necessary action by opening proceedings. In such circumstances, close and constant liaison would replace the referral provision as a method by which a Member State may play a significant role at an early stage in the Commission's decision-making process;
>
> (2) The final decision on any request for referral remains with the Commission;[47]
>
> (3) For an undertaking it is important that only one authority scrutinize any given operation; it is less important which authority. It is therefore vital that the use of the referral provision does not result in the Commission examining one aspect of the concentration, the Member State another. The question arises whether the referral of a notified concentration to a Member State in respect of one local market problem will preclude the Commission from continuing its examination regarding other markets. For example, Company A produces concrete and plaster-board. It merges with Company B, which also produces these two products. The merged undertaking would have a ninety percent share of the southern French concrete market, and an insignificant share of any other concrete market. It would also hold eighty-five percent of the continental plaster-board market.[48] France requests referral of the concen-

46. *Id.* art. 19(2), O.J. L 257/13, at 23.

47. The Commission decision is, however, subject to review by the Court of Justice of the European Communities.

48. The relevant product and geographic markets used in this example are hypothetical assumptions for the purpose of this example alone.

tration regarding concrete in France; should the Commission also open proceedings with respect to the plasterboard market?

Article 9 does not expressly address this point, but implicitly indicates that either *all* of a notified concentration be referred back to a Member State, or none of it.[49] Thus, if a concentration raised local problems in more than one Member State, or if it raised both a local and a Community problem, the Commission would necessarily consider both aspects of the case, and would open proceedings. In any event, it is likely that the Commission will either refer all or none of a concentration on policy grounds, irrespective of any alternative interpretation of article 9 that might militate in favor of the possibility of a partial referral.

The article 9 provision should therefore be seen not as creating a system for multiple control, but as a mechanism for determining which authority is the most appropriate to deal with any particular case. Undertakings may face two or more different authorities conducting inquiries at an initial stage,[50] but in the light of the detailed information that must be provided on notification, this will rarely be substantial.

(4) Relevant geographic markets in the Community are perpetually widening as the principal restrictions to trade—regulatory barriers—fall. Local markets the size of a Member State or smaller will become progressively rarer.

Article 9 also contains provisions to ensure that another of the principles underlying the Regulation—the competition-based nature of the test to be applied—is respected. Article 9(8) provides that the Member State concerned "may take only the measures strictly necessary to safeguard or restore effective competition on the market concerned."[51] In certain Member States, a public interest test is applied to concentrations. This flexible term may include matters not immediately related to a

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49. Article 9(1) states that "[t]he Commission may . . . refer *a* notified concentration." Merger Control Regulation, *supra* note 1, art. 9(1), O.J. L 257/13, at 20 (emphasis added). Article 9(3)(b) states that "it shall refer *the* case to the competent authorities." *Id.* (emphasis added).

50. Inquiries are considered by the Commission prior to the opening of the proceeding, and by the Member State during the three-week period between the date it receives a copy of the notification and the deadline for the submission of its request for referral.

51. *Id.* art. 9(8), O.J. L 257/13, at 20.

competition analysis, such as employment and industrial and regional policy. It is difficult to see how the prohibition of a concentration on such grounds is strictly necessary to safeguard or restore effective competition in the strict sense. However, the Court of Justice has accepted that matters such as social policy are relevant to Article 85(3) of the EEC Treaty, which presumably concerns competition.[52] In light of this the Court will probably allow Member States a wide margin of discretion in determining the meaning of competition, and the measures strictly necessary to safeguard or restore it.

The inclusion of article 9 in the Regulation is therefore welcomed. Its use as a method of providing a certain flexibility for determining which authority is best placed to deal with a concentration is at present limited: any concentration fulfilling the high thresholds in article 1 is likely to have Community-wide effects. However, if the thresholds are reduced to ECU 2 billion by 1993,[53] it will play a role of greater procedural and economic significance.

C. *Referral of a Concentration Without a Community Dimension to the Commission*

The Commission will acquire jurisdiction to adopt the decisions provided for in the Regulation with respect to concentrations without a Community dimension if the following cumulative requirements are fulfilled:

(1) The concentration creates or strengthens a dominant position as a result of which effective competition is significantly impeded;
(2) A Member State explicitly requests the Commission's intervention;
(3) The restriction of competition occurs in, but need not be limited to, the territory of that Member State;
(4) The concentration affects trade between Member States; and
(5) The request is made within one month of the date on which the concentration was made known to the Member

52. *See* Metro v. Commission, Case 26/76, 1977 E.C.R. 1875, ¶ 29, Common Mkt. Rep. (CCH) ¶ 8435, at 7865.

53. The comments of the Commission on the occasion of the adoption of the Regulation indicate that it will present a proposal to the Council along these lines before 1993.

State or was put into effect.[54]

These requirements were included in the Regulation at the request of those Member States lacking developed merger control legislation. They are necessary until the thresholds are reduced, and will disappear from the Regulation once this reduction occurs.

In the event that such a concentration is referred, the Commission may "take only the measures strictly necessary to maintain or restore effective competition within the territory of the Member State at the request of which it intervenes."[55] In most cases, this limitation on the Commission's powers of decision will have little or no effect due to the inappropriate nature of remedies other than outright prohibition or approval in merger control cases.

In the case of trans-border concentrations, this provision does risk creating a multiple system of regulatory control. One Member State may decide to deal with the problem itself, another to refer it to the Commission. If the Commission decided to prohibit all or part of the concentration, its decision would be valid irrespective of a decision by a Member State to clear the operation. Similarly, a Member State's decision to prohibit all or part of a concentration would be valid irrespective of a decision by the Commission not to prohibit. This position is not a deviation from the typical position that a Commission decision takes precedence over a conflicting national one, because the two decisions would aim to remedy a situation in different geographic areas and would not therefore conflict.

Article 9, rather than article 21, creates a real danger of multiple regulatory control with respect to a single concentration. Close and constant liaison between the Commission and the Member States hopefully will reduce such occurrences to the unavoidable minimum, and the coordination of their action will reduce the consequent costs, in monetary and management time, as much as possible.

D. *Protection of the Legitimate Interests of the Member States*

Article 21 permits Member States to "take appropriate

54. *See* Merger Control Regulation, *supra* note 1, art. 22(3), O.J. L 257/13, at 24.
55. *Id.* art. 22(5), O.J. L 257/13, at 24.

measures to protect legitimate interests other than those taken into consideration by this Regulation and compatible with the general principles and other provisions of Community law."[56] It expressly states that legitimate interests include "[p]ublic security, plurality of the media and prudential rules."[57] Before these interests are considered legitimate, however, the Member State must ask the Commission to recognize them as such. The Commission's decision on the legitimacy of such interests must be based on an assessment of their compatibility with Community law.

The effect of article 21 is to partially reverse the normal supremacy principle that a Commission decision or Court judgment in the competition field takes precedence over a conflicting national one. It does not therefore prevent the Commission from adopting any measures provided for in the Regulation in the case of concentration in the armaments or media sectors. It would, however, permit Member States to take a contrary view to that of the Commission on grounds unrelated to competition, which would have precedence. For example, the Commission might find the purchase of a Spanish news agency or weapons manufacturer by a South American company compatible with the competition-based test of the Regulation. The Member State may, however, validly prohibit its completion on other legitimate interest grounds.

A statement by the Commission upon the adoption of the Regulation explains that:

> (1) the provision recognizes the existing reserved powers of the Member states to intervene on grounds other that those covered by the Regulation. Competition related considerations cannot therefore be legitimate interests.
> (2) The clause only enables Member States to prohibit a concentration or make it subject to additional conditions and requirements. It does not enable them to authorize a concentration prohibited by the Commission.
> (3) Prohibitions or restrictions placed on concentrations may constitute neither a form of arbitrary discrimination nor a disguised restriction on trade between Member States.
> (4) Measures will only be compatible with Community law

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56. *Id.* art. 21(3), O.J. L 257/13, at 24.
57. *Id.*

if they are based on the principles of necessity or efficacy and proportionality. The measures taken must therefore be limited to the minimum necessary to ensure the protection of the legitimate interest in question. Where alternatives exist, the least restrictive measure available to achieve the end pursued must be selected.
(5) The term public security is wider than defence interests. Irrespective of the existence of article 21, a Member State may intervene in respect to a concentration that would be contrary to the essential interests of its security and is connected to the production and sale of armaments pursuant to Article 223 of the EEC Treaty. The wider meaning of public security could, for example, cover the need to maintain supplies of strategic materials or other materials necessary for the public good.
(6) Prudential rules relate in particular to financial services and are normally entrusted to national bodies regulating financial markets. They might permit the prohibition of a concentration on the grounds that the acquiring undertaking fails to meet minimum standards regarding the good repute of individuals and solvency requirements.

Although the results of the application of article 21 may result in more than one authority examining a concentration, it does not breach the basic single regulatory control principle. The important point is that any single concentration is examined by a sole competition authority. In all jurisdictions a different number of rules apply to control concentrations, and may be enforced by differing bodies. Their application and implementation requires differing expertise and criteria. Stock exchanges and national banks may, for example, have authority to decide on solvency questions. The Merger Control Regulation provides a system no different to that of such national jurisdictions in this respect.

E. *The Application of Articles 85 and 86 of the EEC Treaty*

The dis-application of the regulations providing a procedural framework for the Commission's implementation of Articles 85 and 86 to concentrations renders the Commission effectively powerless to apply the EEC Treaty's competition rules to concentrations with or without a Community dimension.[58]

On the occasion of the adoption of the Regulation, the Commission reserved the right to take action pursuant to Article 89, but stated that it did not intend to take action in respect to concentrations with a worldwide turnover of less than ECU 2 billion and a Community turnover level of ECU 100 million. Article 89 was intended to provide an interim method to enable the Commission to apply Articles 85 and 86 during the short period between the entry into force of the EEC Treaty and the adoption of detailed procedural implementing rules by the Council. They establish a procedure wholly inappropriate to merger control cases.[59] The procedural drawbacks may ultimately so outweigh any gains in applying Article 86 to concentrations with or without a Community dimension that the Commission will rarely, if ever, have recourse to Article 89.

Article 86 is, however, directly applicable to national courts even in the absence of Council implementing measures.[60] The Commission has stated that it will not normally intervene via Article 89 in cases where the undertakings concerned have a turnover of less than ECU 2 billion/100 million because a concentration would not normally affect trade between Member States at such levels. Below these thresholds, a national court may well decline a request for the application of Article 86 to a concentration on these grounds. Above the *de minimis* threshold, however, it appears difficult to argue that Article 86 would be somehow inapplicable to concentrations. The Commission's explicit desire for a reduction of the thresholds to the *de minimis* level indicates its view that concentrations in this area are likely to affect trade appreciably. It thus appears that, at least with respect to concentrations between ECU 2 billion and ECU 5 billion, a challenge to an operation in a national court under Article 86 has a reasonable chance of success.

58. *Id.* art. 22(2), O.J. L 257/13, at 24.

59. If the Commission finds an infringement, it issues a recommendation, proposing appropriate measures to bring it to an end. If the infringement is not brought to an end, the Commission issues a reasoned decision. The Commission may then authorize Member States to take the measures, the conditions and details of which it shall determine, needed to remedy the situation.

60. *See* Ahmed Saeed v. Zentrale, Case 66/86, 1987 E.C.R. 3801, Common Mkt. Rep. (CCH) [1989] 2 CEC 654.

This interim position will be remedied once the thresholds have been lowered. Article 86 will then be effectively inapplicable regarding concentrations. If the Commission is charged with deciding whether a concentration creates or strengthens a dominant position under the Merger Control Regulation, it is unlikely that a national court will come to a view contrary to that of the Commission by applying Article 86. The problem of the applicability of Article 86 to concentrations below the lowered thresholds will remain, but if the Court of Justice confirms the Commission's position on the absence of an appreciable effect on trade between Member States for such operations, this "infant disease" will be all but remedied.

CONCLUSION

This Article set out to justify the following two statements:

> (1) The exceptions to the "one-stop shop" are of limited importance and based on solid economic reasoning. Furthermore, if intelligently applied by the relevant authorities and institutions, they will not result in the exercise of more than one remedy to any given concentration within the Community.
>
> (2) The Regulation applies only to concentrations, not structures by which independent undertakings co-ordinate their commercial activities. This distinction is valid, taking account of the structure of the competition rules in the EEC Treaty. The test applied to distinguish between the two concepts makes economic and legal sense. The distinction is not difficult to apply in practice.

It failed. Partially.

Firstly, the idea that the "one-stop shop" principle is subject to only very limited exceptions that do not create multiple regulatory control with respect to any particular operation but serve only to determine which authority is responsible for any case is flawed because: (1) the referral of a concentration without a Community dimension to the Commission by a Member State risks the consequence of multiple control; (2) Article 86 may be applied by a national court to a concentration without a Community dimension which is also being examined by a national competition authority; and (3) the existence of the legitimate interest provision.

However, such over-lapping will occur very rarely. The first exception is likely to disappear once the thresholds have been lowered, as it is hoped, will the second. The third is an unavoidable consequence of the lack of political integration in the Community but may become progressively less important if the Community becomes a more political union than it is presently.

Secondly, the test in the Regulation to delineate between coordination and concentration is necessary in the light of the different procedures and remedies under Articles 85 and 86 and the Merger Regulation, and makes economic sense. However, if the Notice were to be seen as giving a severe interpretation of the "autonomous economic entity" test contained in the Regulation it would be more difficult to equate with the economic background, and would risk creating a substantive test in itself.

The factors listed in the Notice should therefore be considered as points to take into account in determining whether or not, in any particular case, an autonomous economic entity (or a permanent structural change) exists, and should not be considered to be a further, additional test, to that of autonomy.

When examined in the light of alternatives, the use of a strict test with detailed guidelines is as clear as could be hoped for. Nevertheless, the distinction will be difficult to apply in practice, not due to a fault in the provisions of the Regulation or the Notice, but to the inherent difficulty of determining whether, as a question of fact, any given operation will affect the competitive relationship between the parents.