mcmillan

Reply to the Attention of	A. Neil Campbell Casey W. Halladay
Direct Line	+1.416.865.7025 +1.416.865.7052
Email Address	neil.campbell@mcmillan.ca casey.halladay@mcmillan.ca
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VIA FAX to + 49 228 9499 400 and EMAIL to konsultation@bundeskartellamt.bund.de and andreas.mundt@bundeskartellamt.bund.de

Andreas Mundt
President
Bundeskartellamt
Kaiser-Friedrich-Strasse 16
53113 Bonn
Germany

Theodor Thanner
Director General
Bundeswettbewerbsbehörde
Praterstrasse 31
1020 Vienna
Austria

Dear President Mundt and Director General Thanner:

Re: Public Consultation — Joint Guidance on New Transaction Value Threshold in German and Austrian Merger Control

We write on behalf of the Merger Streamlining Group ("MSG" or the "Group"), whose membership consists of multinational firms with a common interest in promoting the efficient and effective review of international merger transactions.[1] The cornerstone of the Group's activity has been to work with competition agencies and governments to help implement international best practices in merger control. In particular, the Group focuses on the *Recommended Practices for Merger Notification Procedures* of the International Competition Network ("ICN"), of which both of your agencies are longstanding members.[2]

The MSG was founded in 2001. Its work to date has included two major surveys on implementation of the *Recommended Practices*, as well as more than 50 submissions to the European Commission, the U.S. Antitrust Modernization Commission, and competition agencies and governments in more than twenty other jurisdictions (*e.g.*, the United Kingdom, France, Spain, Italy, Russia, Brazil, India, China, Japan, and Korea) to promote reforms consistent with the *Recommended Practices*, including prior submissions to each of the Bundeskartellamt ("BKartA") and the Bundeswettbewerbsbehörde ("BWB").

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[1] The current members of the Group include Accenture, BHP Billiton, Bosch, Chevron, Cisco, Danaher, General Electric, Novartis, Oracle, Procter & Gamble, Siemens, and United Technologies.

[2] International Competition Network, *Recommended Practices for Merger Notification Procedures*, available online at <http://www.internationalcompetitionnetwork.org/ uploads/library/doc588.pdf> ("*Recommended Practices*").

We write in connection with the public consultation document entitled "Guidance on Transaction Value Thresholds for Mandatory Pre-merger Notification" (the "*Guidelines*") jointly-prepared by the BKartA and BWB.[3] The Group commends both agencies for their ongoing interest in improving the merger control processes in Germany and Austria, and for your willingness to consult with stakeholders on these important issues. The preparation of an English-language courtesy translation of the *Guidelines* is particularly appreciated.

The Group appreciates the depth and level of detail that the *Guidelines* provide on a number of important issues. However, we believe that there are several areas in which the *Guidelines* could be clarified or further improved, as explained in greater detail below. We hope that this submission, which draws upon the MSG members' very substantial experience with multinational merger transactions, will prove useful to you.

I. General Observations and Guiding Principles

While the Group appreciates that both Germany and Austria have already taken the decision to enact transaction value-based merger notification thresholds, we nevertheless think it important to recognize some of the key guiding principles of the ICN's *Recommended Practices* that have particular application to such thresholds, and therefore also to the draft *Guidelines* by which the BKartA and BWB propose to apply their new thresholds.

We begin by noting one of the most axiomatic of the *Recommended Practices*, that "*[m]erger notification thresholds should incorporate appropriate standards of materiality as to the level of 'local nexus' required for merger notification*" and that, when establishing new thresholds, "*each jurisdiction should seek to screen out transactions that are unlikely to result in appreciable competitive effects within its territory*."[4] At explained in greater detail at Part III below, the Group believes that certain aspects of the discussion of what may constitute "*substantial domestic operations*" would lead to the notification of transactions in Germany or Austria that are not likely to have "*appreciable competitive effects*" in those jurisdictions. As the *Recommended Practices* acknowledge, requiring *ex ante* notification of such transactions "*imposes unnecessary transaction costs*" on merging parties and requires the "*commitment of competition agency resources without any corresponding enforcement benefit.*"[5]

The *Recommended Practices* also caution that "*notification requirements and/or practices should be implemented so as to avoid imposing unnecessary burdens on parties to transactions that do not present material competitive concerns*."[6] Many aspects of the analysis

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[3] Bundeskartellamt and Bundeswettbewerbsbehörde, *Guidance on Transaction Value Thresholds for Mandatory Pre-merger Notification (Section 35 (1a) GWB and Section 9 (4) KartG)* (courtesy translation of 14 May 2018), available online at <https://www.bundeskartellamt.de/SharedDocs/Meldung/EN/Pressemitteilungen/2018/14_05_2018_TAW.html;jsessionid=B7CE6CCDE1CA0D2E21D087E5AB08B1E7.2_cid387>.

[4] *See Recommended Practice* I.B, and *Recommended Practice* I.B, Comment 1.

[5] *Recommended Practice* I.B, Comment 1

[6] *Recommended Practice* V.B.

of the value of consideration of a transaction, or of the assessment of substantial domestic operations, set out in the *Guidelines* appear to require highly-detailed, and potentially costly, assessments to be carried out (and extensively documented) by merging parties simply by virtue of the fact that they are entering into a transaction that may be valued in excess of €400 million.

Generally, we note that adopting an expansive approach to interpreting the new notification thresholds (and, in particular, the substantial domestic operations requirement) risks having a "chilling effect" on the acquisition of companies involved in early stage/innovative products (given the additional costs, burdens and delays which a merger control filing may occasion), and therefore in the long term on the incentives to establish and invest in such activities in Germany or Austria (as the prospect of exiting newly-established entities is an important driver for, for example, start-ups or biotech companies).

II. Assessment of the Value of Consideration

The Group applauds the many helpful clarifying statements made in Part C of the *Guidelines* on the subject of assessing transaction value, and in particular those statements indicating that:

- The value of consideration assessment relates only to the assets and/or shares being acquired in the pending transaction, and not to assets or shares previously acquired in the target business.[7]

- Only the interest-bearing portions of any liabilities assumed by the buyer are to be included in the value of the consideration,[8] and where a buyer purchases less than 100% of the target, the value of such liabilities is to be reduced accordingly.[9]

- Transaction-related costs such as legal fees, commission payments to investment banks, and fees for the provision of capital are excluded from the value of the consideration.[10]

The Group believes that paragraph 34 of the *Guidelines* provides an essential clarification to merging parties, by explicitly stating that:

> *If the value of the consideration for a merger project was determined according to this guideline and the merger was considered exempt from notification as a result, the notification requirement will not be reinstated if the components of the*

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[7] *Guidelines*, *supra* note 3 at paragraph 13.

[8] *Ibid.*, at paragraph 16.

[9] *Ibid.*, at paragraph 50.

[10] *Ibid.*, at paragraph 17.

> *consideration value that had already been taken into account* ***change in value after the merger is put into effect*** *[…] If the value exceeds the thresholds later, i.e. after the merger is put into effect, this will* ***not constitute an infringement of the*** *standstill obligation.*[11]

We encourage the BKartA and BWB to retain this analysis in the finalized *Guidelines*, and to consider whether it is appropriate to highlight this important observation in the introductory sections of the document, rather than referring to it in the first instance only at paragraph 34.

The Group believes that the *Guidelines* would be improved by including a discussion of the applicable timeline that is required to treat multiple transactions as a single, consolidated transaction for assessing the value of consideration. For example, at paragraph 13, the *Guidelines* state that "*[i]ndividual acquisitions that are closely connected in material terms and timing have to be regarded as a single merger project for the calculation of the consideration value and for the examination of the merger.*"[12] Example 1b then discusses a hypothetical transaction in which a 25% shareholder of a company acquires a further 26% of its shares through "*two legally separate acquisitions involving two independent sellers each selling their 13% share*", and concludes that "*[t]he two acquisitions of 13% each are closely connected with each other and must therefore be assessed together to calculate the consideration value.*"[13]

While it may be appropriate to consolidate transaction values in two or more separate transactions that involve the same vendor or are otherwise related (for example, because they share a common closing timetable or have other important shared transactional or temporal elements), consolidating transactions that are not related or that are separated by a significant length of time (for example, several months) is inappropriate. In addition to expanding the application of the transaction value notification threshold in an unwarranted manner, this approach will raise significant logistical issues for purchasers in trying to make an *ex ante* assessment of the applicable consideration value.

The Group also believes that the *Guidelines* do not provide a workable approach to the issue of when the consideration assessment — and thus the decision on whether a transaction must be notified in Germany or Austria under the new thresholds — is to be made. At paragraph 27, the *Guidelines* state that "*[t]he relevant factor determining whether a merger project has to be notified is* ***the completion date of the merger***.*"*[14] With respect, we do not believe that this is practical or feasible. As the *Guidelines* recognize on multiple occasions, the value of consideration in a transaction may fluctuate for a variety of reasons between the date that a purchase price is agreed and the date that the transaction closes. Leaving the issue of deal

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[11] *Ibid.*, at paragraph 34 (emphasis in original).

[12] *Ibid.*, at paragraph 13 (emphasis added).

[13] *Ibid.*, at Example 1b, page 5.

[14] *Ibid.*, at paragraph 27 (emphasis in original).

valuation — and thus, by necessary implication, the notification analysis — to the date of closing will create significant uncertainty for merging parties, who may be faced with a notification obligation (and a statutory standstill obligation) that could be triggered at the closing date. The unexpected delay of the closing date in such a circumstance could have range of harmful effects on the financing, tax planning, accounting and other important elements that drive transaction timing.

Instead, the Group respectfully recommends that the BKartA and BWB adopt a fixed date in advance of closing on which the consideration value (and thus, the notifiability) of the transaction would be assessed. As a matter of principle, using the date of the agreement between the parties is an objectively-determinable approach that is likely to most accurately reflect the value that each party believes it has agreed to pay or receive. Importantly, it also allows the process of identifying and preparing the requisite merger control filings to begin immediately.

III. Assessment of Substantial Domestic Operations

Part D of the *Guidelines* deals at length with the important question of what constitutes "*substantial operations*" in Germany and Austria, which is a core element of the notification analysis under the new transaction value-based thresholds in both jurisdictions (and is particularly important given that the *Guidelines* make clear that there is no distinction between "domestic" and "foreign" components of transaction values). While many important guiding principles are provided in this section of the *Guidelines*, the Group has noted below several areas where further information or clarification would substantially improve the *Guidelines*.

At the outset, we note the important reference (at paragraph 62) that "*domestic activity* […] *has to be measured on the basis of the market-related activities of the target company*."[15] While we believe that the *Guidelines*' use of the words "*target company*" implies this, the Group believes that paragraph 62 would be improved by explicitly clarifying that the domestic activity element of the notification analysis should be confined to the particular assets being acquired from the vendor, and not the entirety of the vendor's business. This will provide important certainty to merging parties in a manner consistent with the ICN *Recommended Practices*, which emphasize that notification thresholds should "*be confined to the relevant entities or businesses that will be combined in the proposed transaction*"[16] and that "*the relevant sales and/or assets of the acquired party should generally be limited to the sales and/or assets of the business(es) being acquired.*"[17]

Paragraph 67 incorporates a temporal element, indicating that "*[d]omestic activity must be a* ***current activity***", that "*the point of reference is not the last full financial year preceding the merger but the target company's activity at the point of notification*", and that

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[15] *Ibid.*, at paragraph 62.

[16] *See Recommended Practice* I.B, Comment 3 (emphasis added).

[17] *Ibid.* (emphasis added).

"*[f]uture or anticipated activities are not sufficient*".[18] This is helpful clarification, but the Group suggests that this paragraph be altered slightly to revise the words "*at the point of notification*" to "*at the time of closing*" or, consistent with the point we have made at Part II above, "*as of the date of the purchase agreement*", as most transactions will not require notification.

Another area in which the *Guidelines* would benefit from further clarification relates to applying the concept of domestic significance to transactions in the digital sector. Paragraph 64, for example, states that the number of monthly active users, or the number of unique website visits, in Germany or Austria, could be used as metrics for measuring the "*significance*" of a target company's operations in either country.[19] At paragraph 85, the *Guidelines* provide a case example in which the presence of more than one million users of a particular smartphone app in Germany, or 100,000 such users in Austria, would result in a notification under the new thresholds due to "*the ratio between users and consumers in both countries*."[20] At paragraph 92 a similar case example is given, in which the presence of 70,000 Austrian users of another smartphone app, and one million German users, indicates that "*the significance threshold has been exceeded in both countries*."[21]

The Group believes that the *Guidelines* would be greatly improved if these two very similar examples could be expressed in quantitative terms to provide the sort of "*bright-line tests*" required by the ICN *Recommended Practices*.[22] For example, the example given at paragraph 85 cites the ratio of users to consumers. We understand that Germany has a population of approximately 80.5 million persons, and Austria a population of approximately 8.75 million persons. While not every person may necessarily be considered a "*consumer*", the ratio of app users to total population in the paragraph 85 example would be approximately 1.2% for Germany and 1.1% for Austria. It is questionable whether such a low percentage could meet the legal requirement of being "*significant*". In any event, if a ratio is to be used for assessing the "*significance*" of domestic activity in digital sector transactions, the *Guidelines* would be improved by the addition of a "*bright-line*" numeric threshold — for example, 10%, 5% or 2% — below which the percentage of users to population is not considered "*significant*". It is otherwise very difficult for merging parties to assess the subjective, and somewhat vague, concept of "*significance*" or whether, as stated at paragraph 69, the target company's products or services "*are taken up to a significant extent by domestic users*."[23]

In addition to the digital sector, the *Guidelines* deal at some length with the

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[18] *Supra* note 3, at paragraph 67 (emphasis in original).

[19] *Ibid.*, at paragraph 64.

[20] *Ibid.*, at paragraph 85.

[21] *Ibid.*, at paragraph 92.

[22] *See Recommended Practice* II.A, Comment 1, which states that "*the business community, competition agencies and the efficient operation of capital markets are best served by clear, understandable, easily administrable, bright-line tests*."

[23] *Supra* note 3, at paragraph 69.

pharmaceutical sector. Paragraph 76, and the case example described at paragraph 102, indicate that where R&D activities are carried out[24] in Germany or Austria in respect of pipeline pharmaceutical products in the second or third phase of clinical trials, this is likely to meet the "*significance*" test. Given the high probability of failure of such potential products, the Group respectfully suggests that the *Guidelines* be amended to capture, at most, pipeline products in the third phase of clinical trials (if, on the facts, the acquisition of such products can be said to constitute a concentration). As the European Commission has found on multiple prior occasions, approximately 70% of phase two potential products fail, and the minority of phase two products that are successful still require 4-5 years to reach the market.[25] It is doubtful whether research and development activities in relation to such pipeline products can be said to constitute "*market-related activities*".[26] Moreover, at this nascent stage it will not be clear whether such products, even if ultimately successful, will eventually be commercialized in Germany or Austria and therefore have any domestic nexus in those jurisdictions. The fact that some research and developments activities may take place in, or some assets be located in, a jurisdiction does not necessarily mean that potential products will be approved or ultimately marketed in that jurisdiction.

Requiring *ex ante* notification of the acquisition of such pipeline products, most of which will never be commercialized, would impose a significant and disproportionate burden on merging parties and the reviewing agency with little (or no) corresponding enforcement benefits.[27] For those few potential products that become successful, the market conditions in existence at the time that the BKartA and BWB undertook a merger review will likely have changed significantly following the 4-5 year period required to bring the product to market. The ICN *Recommended Practices* caution that merger notification "*should <u>not</u> be required unless the transaction is likely to have a significant, direct and <u>immediate economic effect</u> within the jurisdiction concerned.*"[28]

Finally, the Group welcomes the statement made at paragraph 79 of the *Guidelines* indicating that "*the Bundeskartellamt will find that there is no significance if the target company generated a turnover below € 5m in Germany and if this turnover adequately reflects its market position and competitive potential*."[29] As noted above, the Group has concerns that aspects of the *Guidelines* discussion of substantial domestic operations are insufficiently clear to meet the "*bright-line tests*" for which the ICN *Recommended Practices* advocate, and the use of a €5 million turnover threshold provides a useful bright-line test.

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[24] We note the comment within paragraph 71 that "*[t]he address details of the inventor of a patent application can also be an indication of the geographical allocation of the research and development activities*." With respect, this is not correct: patent applications are often made at a very early preclinical stage of research and the address details of the inventor will often have no bearing on where an invention will ultimately be further researched developed and commercialized (if at all)

[25] *See, e.g.*, Case COMP/M.1846, Glaxo Wellcome / Smithkline Beecham, at paragraph 70.

[26] *Supra* note 3, at paragraph 62.

[27] *Supra* notes 4 and 5.

[28] *See Recommended Practice* I.C, Comment 1.

[29] *Supra* note 3, at paragraph 79.

However, the value of this bright-line test — and the clarity and predictability that it offers to merging parties — is significantly diminished by subsequent statements in paragraph 79 to the effect that the €5 million threshold will not be applied where "*domestic turnover is not an adequate indicator* […] [and] *the low turnover generated so far does not reflect the competitive potential.*"[30] In the Group's view, the *Guidelines* would be improved by the deletion of this subsequent language limiting the application of the 5 million turnover threshold. In the absence of such a revision, the *Guidelines* should be augmented with a discussion of the types of factors, and further examples, explaining the circumstances in which domestic turnover would not reflect a target company's "*competitive potential*".

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Thank you very much for considering the Group's views. We would welcome the opportunity to respond to any questions or discuss this submission with you or your colleagues further, at your convenience.

Yours very truly,

A. Neil Campbell

Casey W. Halladay

Copy to: Members of the Merger Streamlining Group

[30] *Ibid.*