German Merger Control and International Transactions – Mixed Signals, At Best

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If, as expected, a recent bill finds Parliament's blessing in early 2009, Germany will soon have notification thresholds that relate to the size of each party's presence in Germany (Draft Third Act Reducing Bureaucracy In Particular For Small And Mid-Sized Businesses[1], "ARC Bill"). Currently, almost any cross-border transaction requires merger control clearance in Germany, because typically the involvement of one large party in the transaction is enough to satisfy the current German turnover tests. The ARC Bill, therefore, is certainly good news. Its significance should not be overestimated, however. Other developments demonstrate that the *Bundeskartellamt* (Federal Cartel Office, "FCO"), Germany's principal antitrust authority, will not loosen its grip on international mergers and acquisitions activity.

State of Play

Germany is notorious for its all-encompassing filing thresholds. Transactions have to be filed for the FCO's review if, in the most recent financial year, (i) the parties generated combined revenues of more than € 500 million worldwide and (ii) at least one party generated revenues of more than € 25 million in Germany. "Parties" includes affiliates, and "revenues" must be consolidated on a group-wide basis.

The € 25 million test relates to "one party." It is also fulfilled where only the buyer or only the target has significant operations in the country. Other than the turnover tests discussed above, there is no screen for local nexus, at least not on the basis of how the FCO tends to interpret the law. The ARC provides for an effects-type assessment,[2] but the FCO's broad interpretation of this condition renders it virtually meaningless.

In particular, the FCO takes the position that competition in Germany is affected where both parties have been active in Germany in the past. Where only one party was active in the past, likely future supplies to Germany are sufficient to trigger a filing requirement; a filing also may be required if the transaction is likely to enhance the know-how, IP or financial strength of the party that is active in Germany. For the formation of joint ventures outside of Germany, the FCO assumes that the joint venture affects competition in Germany if the joint venture is active in European or worldwide markets.[3]

As a result, the FCO's workload is impressive. The FCO reviewed a total of 2,240 merger submissions in CY 2007 (1,829 in CY 2006) – a significant number compared to the 2,201 transactions that were reported to the U.S. FTC under the HSR Act in FY 2007 (1,768 in FY 2006). It is also a significant number in light of the fact that parties must provide a substantial amount of market data as part of any filing.

For businesses, the FCO's practice of requiring filings in matters with relatively little nexus to Germany imposes significant burdens on merging parties, including costs and the time required to complete a notification. The FCO's position also imposes another significant burden on parties – legal uncertainty. For instance, at the time the buyer assesses filing requirements, it may not have access to the target's revenue data, or these data may be aggregated in a matrix which does not comply with Germany's rules for allocating turnover geographically. Therefore, a filing requirement in Germany may only become apparent post-closing. Where a transaction requires FCO clearance but clearance has not been obtained, the transaction is not legally enforceable in Germany. To remedy this situation of legal uncertainty, the FCO used to accept post-closing filings but it has discontinued this practice.[4] Today, if the FCO is notified or becomes otherwise aware of the transaction post-closing, it investigates whether the criteria for

[1] BR-Drs. 558/08, August 8, 2008, amending the notification thresholds of Section 35(1) of the German Act Against Restraints Of Competition („ARC").

[2] Section 130(2) ARC.

[3] FCO, Notice Regarding Domestic Effects, January 1999.

[4] FCO, Notice: No Post-Closing Notifications, May 2008.

prohibition are satisfied and, if they are, orders that the merger be dissolved (and it may impose a fine). If the prohibition criteria are not satisfied (and even if the FCO does not impose a fine), there is a risk that the courts will declare the transaction void.

The Proposed New Notification Threshold

Pursuant to the ARC Bill, transactions will only have to be reported if the worldwide-revenues test described above is satisfied and, in addition, (i) one of the parties generated revenues of more than € 25 million in Germany; and (ii) the other party generated revenues of more than € 5 million in Germany.

While this amendment will mitigate the current issue of over-enforcement, it will certainly not eliminate it. First of all, revenues of € 5 million or more in Germany – a country among the top-five worldwide in terms of GDP – are not much of a hurdle. Moreover, the effect that the new threshold will have on the number of filings is quite unclear. The FCO does not publish statistics regarding average deal valuations of transactions requiring notification. The government estimates that the new test will reduce the number of filings by up to one third but does not disclose the statistical basis of its estimate. Arguably, the new threshold would have to be much higher to generate the targeted reduction factor of one third. The supporting memorandum of the ARC Bill is anything but helpful in this regard. It refers to the aim of reducing "red tape" in Germany; in particular, for small and medium-sized businesses. However, transactions involving only small and medium-sized businesses are unlikely to satisfy the € 500 million threshold in the first place.

In any event, the FCO will need to provide continued guidance to merging parties, notwithstanding the changes to its notification standard. For instance, the new test refers to "two" parties to a transaction, but it is not clear how this test relates to joint ventures, which can involve any number of parties. If there are two joint venture parents with German revenues above the new thresholds, the formation of the joint venture would have to be reported in Germany even if the venture will have no sales in Germany. Hopefully, therefore, the FCO will not interpret the new test as Germany's final and conclusive comment on the issue of extra-territorial jurisdiction.

The recent past does not suggest that the FCO will offer much leeway to non-German parties to a transaction that have little presence in Germany. On the contrary, there has been a significant increase in the number of prohibitions of transactions where the parties were non-German corporations and the transaction was completed abroad.[5] Moreover, the FCO has proven to be entirely unimpressed with the substantive position that other antitrust authorities, including the U.S. agencies, have taken towards the transaction it is reviewing.

Additional Regulatory Requirements

Going forward, the FCO may not be the only agency which takes an interest in transactions filed in Germany for antitrust review. Parliament is considering a bill that will introduce a new power for the government to prohibit the acquisition of shares in German companies by non-EC companies where it finds that the transaction would put the public welfare at risk (Draft 13th Act Amending the Foreign Trade And Payments Act and Regulation[6], "FTPA Bill"). The government will have this power if (i) the share ownership of a non-EC acquirer will increase above 25%; and (ii) the acquisition would create a risk for Germany's "order or security."

Similar powers over transactions already exist today but are limited to those involving certain industries such as defense, cryptographic systems, and certain high-tech satellite surveillance systems. The FTPA Bill, by contrast, does not limit the types of industries to which the government's powers to block a transaction would apply. In particular, in-bound investments in national champions, telecom companies and electricity/gas businesses may be candidates for review. Notably, an acquirer would qualify as a non-EC company under the FTPA Bill where it is a German (or EC company) but has a non-EC shareholder owning more than 25%. The government will have three months post-transaction to decide whether to investigate and, if it does, two additional months to prohibit it. The new power will be linked to Germany's merger control system. The FCO will report the information it receives on transactions to the Ministry in charge of applying the new provision.

[5] FCO, March 24, 2004, WuW DE-V 931 – *Synthes-Stratec/Mathys*; October 25, 2006, WuW DE-V 1325 – *Coherent/Excel*; February 14, 2007, WuW DE-V 1340 – *Sulzer/Kelmix*; April 11, 2007, WuW DE-V 1365 – *Phonak/GN ReSound*; August 24, 2007, WuW DE-V 1442 – *Kalmar/CVS Ferrari*.

[6] BR-Drs. 638/08, August 29, 2008.

The ARC Bill will reduce the number of transactions to be filed for FCO review. For those transactions submitted for review, the FTPA Bill may increase the risk of governmental intervention. However, issues regarding the government's new power to control in-bound investments will likely be settled politically rather than through formal administrative processes.