INTERNATIONAL BAR ASSOCIATION
ANTITRUST COMMITTEE'S
COMMENTS ON THE DRAFT GUIDANCE OF THE
BUNDESKARTELLAMT AND THE BUNDESWETTBEWERBSBEHÖRDE ON
TRANSACTION VALUE THRESHOLDS FOR MANDATORY PRE-MERGER NOTIFICATION
(SECTION 35 (1A) GWB AND SECTION 9 (4) KARTG)

June 15, 2018

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1. INTRODUCTION

1.1 On May 14, 2018, the German Bundeskartellamt ("**BKartA**") and the Austrian Bundeswettbewerbsbehörde ("**BWB**") (jointly, the **"Agencies"**) published their joint draft Guidance on Transaction Value Thresholds for Mandatory Pre-merger Notification (Section 35 (1a) GWB and Section 9 (4) KartG) (the **"Draft Guidance"**). These comments have been prepared by the Merger Working Group (**"MWG"**) of the Antitrust Committee ("**Committee**") of the International Bar Association (**"IBA"**).

1.2 The IBA is the world's leading organization of international legal practitioners, bar associations and law societies. The IBA takes a keen interest in the development of international law reform and helps shape the future of the legal profession across the globe. It is the global voice of the legal profession.[1]

1.3 The IBA has 80,000 individual lawyer members from around the world, including many from Germany and Austria. The IBA's Antitrust Committee includes competition law practitioners with a wide range of jurisdictional backgrounds and professional experience, which places it in a unique position to provide international and comparative analysis in the development of competition laws and enforcement practices.[2]

1.4 The Committee maintains working groups which provide input on the development of competition laws around the world, including the MWG. Having regard to its interest in important international legal developments in significant jurisdictions such as Germany and Austria, and having provided comments to the German Ministry of the Economy during its consultations regarding the adoption of the transaction value thresholds, [3] the Committee respectfully submits its comments and suggestions on the Draft Guidance.

1.5 The Committee welcomes the willingness of both Agencies to provide guidance on the application of the transaction value thresholds for mandatory pre-merger notification enacted in 2017 in Germany and Austria. Such guidance will be beneficial to both the Agencies as well as to parties to M&A transactions and their advisors, both local and international. The Committee considers that the Draft Guidance provides sophisticated and substantial guidance and would like to assist the BKartA and the BWB in providing even more precise and useful guidance.

1.6 The Committee also believes that it is important for the Agencies to recognize the important function of German and Austrian competition law and administrative practice as a point of reference for other, younger jurisdictions. Decisions taken in Germany and Austria – at legislative

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1 Further information about the IBA is available at http://www.ibanet.org/.

2 Further information about the IBA Antitrust Committee can be found at http://www.ibanet.org/LPD/Antitrust_Trade_Law_Section/Antitrust/Default.aspx

3 See https://www.ibanet.org/LPD/Antitrust_Trade_Law_Section/Antitrust/Publications.aspx

as well as administrative levels – have an impact that goes far beyond the direct reach of German and Austrian law. The Committee considers that it is important to keep this in mind when applying the new transaction value thresholds – if Germany or Austria decides to cover transactions with hardly appreciable domestic effects, other countries may be motivated to follow suit. This could potentially have negative impacts on German and Austrian as well as international M&A activities.

1.7 The Committee offers these comments in the spirit of constructive input and hopes that the Agencies will find this contribution to be helpful in the development of sound competition policies and administrative practices for merger control.

2. SCOPE AND APPROACH OF THE DRAFT GUIDANCE

2.1 The new provisions on transaction value threshold values are intended to adapt competition law to economic changes due to technical developments and globalisation. The new thresholds in Section 35 (1a) GWB and Section 9 (4) KartG cover cases where current turnover and the purchase price for the target (regardless of where it is located and how many countries it is active in) differ to a significant and disproportionate extent. The new thresholds are subsidiary to the turnover-based criteria of Section 35 (1) GWB and Sections 9 (1), (2) and (3) KartG and do not affect the practical application of the turnover-based criteria.

2.2 The new thresholds were designed to allow German and Austrian merger control rules to catch transactions that may have an impact on competition with regard to an acquired firm's potential – and in particular future - capability, rather than its actual performance based on turnover. While the high purchase price in such transactions may be an indication of innovative business ideas with significant competitive market potential, the MWG expects that only in rare cases will there be a lessening of competition that contravenes substantive merger control laws (just as the vast majority of mergers reviewed under turnover-based thresholds in virtually every merger control system in the world are determined not to be anticompetitive[4]). In fact, the new thresholds by design aim to capture innovative start-up companies that often as a business model will seek to monetize the investment by way of selling the operations. As such, the new thresholds might dampen innovation by constraining start-ups to monetize on their innovations. This may lead to a situation where the new tests lead to welfare-reducing effects which eventually outweigh the benefits of capturing few isolated cases that potentially might impact competition. Thus, the MWG believes that it is vitally important to ensure that the new transaction value thresholds are applied in a way that is cautious, transparent, and practical while minimising unnecessary compliance burdens.

2.3 The Draft Guidance is based on the first experiences of the Agencies with the new thresholds. It is meant to provide users with guidance applying the new provisions and focuses largely on the determination of the value of the consideration and the definition of substantial domestic operations, and also briefly considers the definition of concentration. These comments follow the same structure.

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4 For instance: In Austria, 99% of all notified cases within the last three years were cleared in phase 1 (source: Tätigkeitsbericht, BWB, 2017). In Germany around 93-95% of all notified cases in 2015 and 2016 were cleared in phase 1 (source: Tätigkeitsbericht, BKartA 2015/2016, p. 140).

3. VALUE OF THE CONSIDERATION

3.1 While in general it should be less problematic to apply the value-based thresholds to transactions with a fixed purchase price that is payable at closing, [5] uncertainty will arise in transactions where it may be difficult to determine the transaction value precisely. This may be the case for transactions where the value of consideration depends on certain conditions being met (e.g. earn-out arrangements or material purchase price adjustments), where it will be determined partially at a later point in time, or where it takes the form of options to receive the acquirer's shares in the future. To evaluate such situations, the MWG proposes that the value of consideration test will (as far as possible) draw upon established methods such as the U.S. size-of-transaction test.[6] However, the Agencies are proposing a different approach in several aspects, which has created uncertainties amongst practitioners since the entry into force of the new thresholds. The Draft Guidance is a commendable attempt to clarify many issues, but still raises several questions as to the practicability and burden of the proposed calculations. Clear rules should be provided to reduce such uncertainties. Otherwise, merging parties may – erring on the side of caution – choose to submit filings for transactions in order to avoid any possible risks, thereby adding burdens to both themselves and the Agencies; or (notably in foreign-to-foreign mergers) erroneously overlook a filing obligation if rules are unclear or overly complex. Below the MWG discusses several specific areas where it considers that the guidance could be improved.

3.1.1 **Fixed future payments (para. 11).** Transactions involving companies with a low turnover, but substantial growth potential, may include future payments that are specified in the transaction agreements. The Draft Guidance encompasses such future payments as an element of the value of consideration.[7] Such future payments are often dependant on certain conditions being met, but may also be pre-set at precise amounts agreed at the time of the transaction. It would be desirable to recognise this distinction and explicitly specify that the value of consideration should include such agreed fixed future payments. However, the Draft Guidance should elaborate on how payments which are conditional will be treated, as well as items such as fixed contractual penalties for not reaching targets (i.e. deductions from the purchase price), and should consider whether it is appropriate to discount those future payments to their net present value for purposes of the valuation.

3.1.2 **Unrelated 3rd party agreements (para. 11 et seq.).** To induce the development of a company or its products, investors often include bonuses and future payments conditional on the achievement of certain targets, such as sales, R&D, or customer base. The Draft Guidance includes future and variable purchase price components as elements of the value of consideration, and focuses on elements being directly linked to the acquired undertaking.[8] The Draft Guidance does not consider cases where future payments are not

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[5] One of the matters not resolved by the Draft Guidance is the determination of the transaction value in cases where the purchase price is payable in a foreign denomination subject to strong exchange rate fluctuations. For the sake of legal certainty and practicability, it seems advisable to (exceptionally) determine the time of signing as the relevant valuation date rather than the date of closing (see also 3.1.8.).

[6] Such as the acquisition price and fair market value.

[7] See para. 11 of the Draft Guidance.

[8] See para. 15 of the Draft Guidance, where elements of future price components include company parameters and conditions, including sales, earn-out payments, drug approval.

merger specific, but where they are dependent on separate agreements, such as supply relationships with vendors or other third parties. In the MWG's view, the value of such agreements should not be included when determining the consideration for the assets or entity being acquired since they relate to additional purchases of goods or services.

Closely connected to these kind of the aforementioned agreements but so far not considered in the Draft Guidance are additional commercial agreements entered into between the acquirer and the target, e.g. for the supply of goods which are not necessarily (legally) conditional upon the transaction but are agreed in parallel or in a close temporal and factual link to the transaction. Here the question arises if budgeted or expected sales from a business plan should be part of the value of the consideration. Such investment scenarios often occur when venture capital companies or venture capital arms of large groups invest into start-up companies often in several consecutive investment series. Mostly, such investments are designed in a way that non-controlling minority shareholdings below 25 % are acquired but they could qualify for the acquisition of a competitively significant influence within the meaning of Section 37 (1) No. 4 GWB. In the MWG's view a clarification on such transaction scenarios would be greatly appreciated. If the BKartA and the BWB were of the opinion that such agreements may also be covered by the value of consideration it should be clearly stated what are the criteria for a close temporal and factual link to the transaction. If at all, in the MWG's opinion, the date of signing should be a clear cut off date (only evident abusive cases may be exempt of this rule). Any commercial agreements after this date should not be taken into account for the sake of legal certainty.

3.1.3 **Confirmation of value (para. 20 et seq.).** As a general remark, even binding confirmations of good faith determinations of consideration by an undertaking's management should not be subject to enforcement consequences for the involved individuals in cases of accidental incorrect statements. For the value of future purchase price components, internal assumptions concerning the expected future value can be subject to a confirmation that cannot predate the notification by more than 90 days, including the amount of the value and assessment method.[9] If necessary, the parties seem to be able to additionally present a valuation report that can predate the notification by six months or more.[10] The Draft Guidance could further clarify whether the aforementioned confirmation could simply confirm the accuracy of an older report, or otherwise further elaborate on the expected scope of such a confirmation.

3.1.4 **Assessment by acquirer and seller (para. 21 et seq.).** The Draft Guidance suggests that both the acquirer and seller provide individual estimates for the valuation of future and variable purchase price components.[11] The intention seems to be to enable a balancing assessment between the two parties. Also, it is supposed to facilitate cases where it is uncertain whether the value exceeds the threshold of €200m under Section 9 (4) KartG or €400m under Section 35 (1a) GWB. However, this provision would ultimately create more of a burden than actual utility for the authorities' assessment. To begin with, it

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9 See para. 20 of the Draft Guidance.

10 See para. 22 of the Draft Guidance.

11 See para. 21 of the Draft Guidance.

would be duplicative and wasteful to require both parties to conduct separate valuation analyses. Secondly, given that the Draft Guidance does not set precise requirements as to the methodology of estimating future value, it is not unconceivable that for most transactions the Agencies may ultimately be dealing with the assessment of two entirely separate estimates, the comparison of which could be complicated (such as in the case of incongruent market analyses regarding the future growth prospects). Additionally, the acquirer and seller often may have conflicting business interests or perspectives which may render the valuations even more complicated. For instance, a strategic buyer might gain synergies by combining businesses beyond a scale that the seller could achieve, and consequently valuate the target business higher than the seller. Here, the question arises as to how the authorities would deal with a situation, where the acquirer's valuation remains under the thresholds, but the seller's valuation places the transaction above the thresholds. If the authority were to claim a filing requirement on the basis of the seller's valuation, what information would the authority provide to the acquirer upon a request to understand the different outcome? Diverging valuation methods between the seller and the acquirer can be of vital importance for commercial negotiations. As such, the requirement for two separate valuations could ultimately lead the authorities to interfere with strategic commercial interests of the parties. Moreover, the parties may not want or be able to share their internal valuation estimates with each other. The Draft Guidance should therefore be revised to exceptionally place the responsibility for valuation solely on the acquiring party.

3.1.5 **Flexible level of assessment details (para. 27 et seq.).** Overall, it should be pointed out that requiring value assessments can often involve considerable effort, time and cost for the parties, including possibly the engagement of external specialists (which the Draft Guidance seems to encourage, rather than limiting to situations where it may be essential). The Draft Guidance generally seems to distinguish between the scenarios where a transaction's value would clearly exceed or fall below the threshold of €200m under Section 9 (4) KartG or €400m under Section 35 (1a) GWB, and transactions where this is less certain.[12] This principle seems favourable and the Draft Guidance could emphasize it in the explanations of the value assessment. In cases where the thresholds clearly are or are not met, the burden on the notifying parties to present the calculation method could be eliminated. This could be reflected in the confirmation requirement in para. 20 of the Draft Guidance. In any event, as explained below, the burden of proof that a notification obligation exists ultimately lies with the Agencies and should therefore not be unduly transferred to the parties.

3.1.6 **Value assessment (para. 27 et seq.).** In its explanations of the value assessment in para. 27, the Draft Guidance could take into account the often burdensome access to the relevant information by the acquirer in order to create a plausible and reasonable future value assessment. To this effect, the authorities could helpfully require that the value of consideration be assessed solely on the basis of information reasonably available to the acquirer exceptionally at the time of signing. Alternatively, in cases in which the acquirer does not have sufficient information or knowledge to conduct a valuation, it could delegate that task to the seller and rely on the seller's valuation. There may also be implications concerning the standstill obligation with such information exchanges that should be discussed in the Draft Guidance.

[12] See para. 27 et seq of the Draft Guidance.

3.1.7 **Probability calculation (para 29 et seq.).** When explaining the calculation of estimated value of consideration based on future payments, the Draft Guidance deals with discount rates in order to leverage the probability of such future value actually occurring.[13] Ultimately, such discount rates are subject to assumptions which must be transparent and plausible. Such an open provision creates uncertainty for parties, which may result in increased precautionary notifications. The Draft Guidance could further elaborate on a number of items in order to provide more accurate instructions for such assumptions, (e.g. reflecting what a willing buyer would pay given a certain scenario on the market, or assessing market predictions with commercially reasonable business development in good faith). It would also be advisable to provide more guidance and examples on the elements of probability assumptions, as well as on the methodology of calculating appropriate discount rates.[14] Furthermore, the Draft Guidance could provide more instructions for acquisitions at below market value, such as bailouts, in particular as regards the required valuation approach and documentation. In general, it would be advisable to not put too much burden on the parties and provide them with a reliable framework as regards their valuation and assumptions. One example could be pre-set standardized probability discount rates for common scenarios. This should reduce uncertainties, minimize unnecessary precautionary notifications, and align valuation methods applied in submissions.

3.1.8 **Change in value (para. 34).** The Draft Guidance deals with "*consequences of a change in value following an examination by the competition authority*".[15] It is unclear whether this relates to the situation where "(…) the merger was considered exempt from notification (...)" in the course of the parties' self-assessment, or – following the reasoning in the title – whether a previous examination (i.e., of a notification requirement) by the authorities would always be required. This should be clarified and explicitly refer to a bona fide self-assessment by the parties. More importantly, the intended triggering event should relate to signing rather than implementation. The parties to a transaction agree on the value and price elements at signing, and possible fluctuations in currency or other external elements should not be the parties' responsibility between signing and closing (or even post-closing for future payments). For example, in the United States, the parties are permitted to rely on good faith fair market valuations as of any day within 60 days prior to the filing or prior to closing if no filing is made regardless of whether future events prove them incorrect. In addition to being contrary to sound principles, a system that bases the value of consideration on the closing date would be uncertain and unpractical for parties conducting M&A transactions. Finally, the Draft Guidance should expressly state that subsequent events not known or foreseeable during the preparation of the value assessment (conducted at the time of signing) should not be taken into account.

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[13] See paras. 29-32 of the Draft Guidance.

[14] The Draft Guidance could use elements from the underlying principles of the fair market value calculation under the HSR rules. The Draft Guidance seems to have already partly applied some of these elements for securities transactions in para. 37 et seq.

[15] See para. 34 of the Draft Guidance.

3.1.9 **Burden of proof (para 46 et seq.).** The MWG supports the view that a properly conducted calculation of the value of the transaction confirmed by the management of the target should result in a presumption of correctness. However, the MWG strongly rejects the notion that may be implied in the Draft Guidance to the effect that the undertakings concerned are required / carry a burden of proof to demonstrate the accuracy of the value of consideration in securities transactions.[16] Although the notifying party's calculation should reasonably explain or confirm the basis of an appropriate value assessment in cases where the notification requirement is contested to avoid possible fines being imposed for negligent non-notification, the Agencies have the burden of proof under the applicable laws to demonstrate that the notification requirement exists – *i.e.*,, that the value of the transaction meets the relevant financial thresholds.. The Draft Guidance should be amended to eliminate this lack of clarity. For example, in the United States, the requirement is for the board of the ultimate parent entity of the acquirer (or its delegee) to make the fair market valuation in good faith as of any day within 60 days prior to the HSR filing or prior to closing if no HSR filing is made. A financial officer of the acquirer who is involved in the transaction is considered a de facto board delegee for these purposes. Following this type of procedure should obviate the need to demonstrate the accuracy of the valuation.

3.1.10 **Assumed liabilities (para. 50 et seq.).** Concerning assumed liabilities, the Draft Guidance quotes Section 38 (4) GWB and the explanatory memorandum in Austria as the basis for, including liabilities assumed as part of the value of the consideration.[17] The addition of liabilities seems to apply to the interest-bearing components of the liabilities only, and would not include non-interest-bearing liabilities (such as payables for goods and services). This narrower approach is favourable, being closer to the U.S. counterpart that does not include assumed debt in the valuation of voting shares or non-corporate interests (although certain assumed liabilities are included in US asset acquisitions).

3.1.11 In particular, according to the Draft Guidance the value of the consideration shall include liabilities in the acquired company (and not only liabilities that were assumed from the seller), even if the target is acquired by way of share deal. Yet, it is not clear why liabilities of the target should be added to the value of the consideration. It contradicts the legal liability regime for (limited liability) companies. As such, the MWG recommends that only liabilities assumed by the acquirer (e.g. by means of an asset deal or debt assumption from the seller) should be added to the value of the consideration. Conversely, liabilities of the target do not increase the value of the consideration. This is also in line with U.S. merger control, where only in case of an asset deal the value of the consideration includes liabilities assumed by the acquirer.[18] The MWG would welcome if the merger control regimes would follow a consistent path in the calculation of the value of the consideration in order to align the jurisdictional approaches and to maximize legal certainty as well as predictability while avoiding unnecessary costs and burdens on the parties.

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[16] See para. 46 of the Draft Guidance.

[17] See para. 50 of the Draft Guidance.

[18] See https://www.ftc.gov/enforcement/premerger-notification-program/hsr-resources/valuation-transactions-reportable-under.

3.1.12 **Amalgamations (para. 56).** The Draft Guidance provides a more detailed view on the assessment of parties within joint ventures, but keeps explanations for the case of amalgamations at a very broad level.[19] If two or more market players intend to set up a new joint venture, the German and Austrian authorities view the parties' respective capital and asset contributions as consideration for the transaction which shall be subject to valuation. As regards amalgamations – except for cases of one company absorbing another – however, it may not be clear who should be regarded as buyer and who as seller, in particular in the case of a formation of a new company. The Draft Guidance recognizes this issue and offers to provide advice on a case-by-case basis. However, it would be preferable to provide more clarity on the assessment of such transactions in general (e.g. by providing examples to illustrate and determine who will be considered as the buyer, at least, in typical transaction scenarios).

3.2 In summary, the MWG believes that the Draft Guidance is a welcome step towards shedding more light on the uncertain metrics behind the value of consideration. It appears to be an attempt to capture dynamic market developments mostly of big technology companies seeking potential growth in the market (although the thresholds may catch many other situations). However, the given value of an undertaking is not the same as its value calculated as a typical investment – as used in the financial industry. Predictability decreases the longer the timeframe that needs to be taken into account. This should be borne in mind and explicitly acknowledged when finalizing the Draft Guidance. In that respect, the use of competing estimates based on unspecified probability-multipliers, chosen by each acquirer (and seller[20]) at their own discretion, neither seems to stipulate a clear and efficient assessment method, nor sufficiently differentiate fluctuating growth-investment bubbles from transactions which actually have potential relevance for competition. As a result, parties are likely to notify unproblematic transactions solely out of precaution or, (especially in foreign-to-foreign transactions) may even overlook a filing obligation. Every foreign party with a deal above these thresholds must assess whether the German and Austrian thresholds will apply (even though much of the deal value will relate to other geographies). The vastness of the jurisdictional claim is an important context point for seeking clear and focused guidance. To avoid these risks, the Draft Guidance should therefore introduce more accuracy and certainty – accompanied by more examples – as regards the different items of the value assessment.

3.3 Given the complexity of the matter and the potential uncertainties inherent in the valuation of transactions, the MWG believes that consultations – which currently seem to constitute only an exceptional instrument in the Draft Guidance – should gain greater prominence. The MWG suggests that the Agencies should introduce a system of binding confirmation requests, which do not require in-depth details of the intended transaction but focus on the question of whether the relevant thresholds are met. This mechanism could on the one hand incentivize parties to actively consider the question which might otherwise "take a view" thereby fostering a culture of compliance and could, on the other hand, reduce the number of precautionary filings that the parties might make, and the related resource burdens on the Agencies as well as the parties.

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[19] See para. 56 of the Draft Guidance

[20] But see the Committee's comments above regarding the irrelevance of seller.

4. SUBSTANTIAL DOMESTIC OPERATIONS

4.1 The Draft Guidelines foresee a three-tier analytical framework to assess whether there is a substantial domestic operation, namely the assessment of the a) local nexus of the activities, b) marketability of domestic activities (also market-orientation) and c) significance of the activities.

4.2 It is stipulated in German (Section 35(1a) no. 4 GWB) and Austrian (Section 9(4) no. 4 KartG) law that a domestic activity of the target (not merely any party to the transaction) is required and that this domestic activity must be *"significant"*. It is important to recognize that the notification and review of transactions which do not have appreciable connections to Germany or Austria would consume valuable resources of the BKartA or the BWB, in addition to placing significant burdens on private parties. The Draft Guidance helpfully emphasizes that the law requires *current* domestic activity at the time of notification and not only expected or intended domestic activity.[21]

4.3 With regard to the necessity of a sufficient or material domestic nexus, the ICN Recommended Practices for Merger Notification and Review Procedures (**"ICN Recommended Practices**", lastly amended in May 2017) provide valuable further guidance. These recommendations require a *"significant and direct economic connection to the jurisdiction*" (i.e. *"significant local sales or local asset levels*")[22] and stipulate that *"jurisdiction should be asserted only with respect to those transactions that have a material nexus to the reviewing jurisdiction*".[23] Either each of at least two parties to the transaction should have significant local activities or (alternatively) the acquired business needs to have a significant presence in the local territory, such as significant local assets or sales in or into the reviewing jurisdiction. The ICN Recommended Practices further emphasize tha*t"[...] the likelihood of adverse effects from transactions in which only one party has a significant local presence is sufficiently remote that the burdens associated with notification are normally not warranted."* [24]

4.4 Another important factor besides a material nexus is that there is sufficient legal certainty as to the requirements for such local nexus. The ICN Recommended Practices emphasize correctly: *"Clarity and simplicity are essential features of well-functioning notification thresholds.*" Therefore, it is necessary to adopt "*clear, understandable, and easily administrable 'bright-line' tests.*"[25]

4.5 Practical considerations are of particular importance for parties to transactions who may be assessing potential filing requirements in a multitude of jurisdictions. The ICN Recommended Practices therefore emphasize that: "*To facilitate the parties' ability to gather multi-jurisdictional data on a consistent basis, jurisdictions should seek to adopt uniform definitions or guidelines with respect to <u>commonly used criteria</u>* (emphasis added)."[26]. Thus, it is also important that the

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[21] See para. 67 of the Draft Guidance.

[22] ICN Recommended Practices, Item II. B., Comment 1.

[23] ICN Recommended Practices, Item II. A., Comment 1.

[24] Cf. ICN Recommended Practices, Item II. C., Comments 1 and 2.

[25] ICN Recommended Practices, Item II. D., Comment 1.

[26] ICN Recommended Practices, Item II. E., Comment 3.

information needed to determine notification thresholds is readily accessible by the parties. Appropriate guidance is necessary on the precise methodology to be applied to assess the indicators identified. These practical considerations must be kept in mind when assessing potential criteria for the measurement of relevant domestic activities. The ICN Recommended Practices rightly stress that *"[m]andatory notification thresholds should be based exclusively on objectively quantifiable criteria* (emphasis added*)."*[27]

4.6 According to the Draft Guidance, if the target exclusively or primarily operates on the domestic market this will generally constitute sufficient domestic operations[28]. The Draft Guidance emphasizes that the measurement of domestic activities requires an *"appropriate indicator"*. However, unlike for the existing turnover-based thresholds, the domestic turnover shall generally not be such indicator. Nonetheless, such turnover may still be a relevant factor in mature markets that are characterized by turnover generation[29]. The Committee considers that this is an appropriate approach to avoid triggering notifications of transactions whose significance can and should be assessed using the normal turnover thresholds.

4.7 The Draft Guidance further elaborates that the measurement of domestic activity shall consider industry standards that "*cannot be easily manipulated*" [30]:

- For the digital sector the amount of (active) customers or frequency of access of a website by customers shall be possible indicators.

- Unlike for Austria, it shall not be sufficient for Germany to refer to the location of the target company, (i.e. whether it has a site in the respective country). The BKartA considers the use of the asset for business activities as a key factor and not the mere local physical location of the asset[31]. In light of the "bright-line" test requested by the ICN Recommended Practices, the Austrian approach seems easier to assess since it might be difficult to precisely attribute the actual use of assets to domestic or other activities. However, especially in the digital world, the mere location of the target does not necessarily entail significant business activity and should therefore be considered as a mere indication.

- For Austria, the Committee would welcome the clarification that a location itself is not sufficient to construe a significant domestic activity, but would need to go along with market-facing operations in Austria in order to trigger the test. Para. 65 of the Draft Guidance could otherwise be misread that even the acquisition of a mere holding entity or foundation located in Austria without any market-facing operations in Austria might trigger the test.[32] Such a wide scope would, in fact, go beyond what would normally be

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27 ICN Recommended Practices, Item II. E., Comment 1.

28 See para. 61 of the Draft Guidance.

29 See para. 62 of the Draft Guidance.

30 See para. 63 of the Draft Guidance.

31 See para. 66 of the Draft Guidance.

32 While the legislative explanatory notes mention a local establishment as a relevant indicator, it transpires from the rationale of the new test that the legislator had an operative (market-facing) business in mind. As

considered to amount to a relevant nexus under the (far-reaching) domestic effects test (Section 24 (2) KartG).

4.8 To assess the **local nexus** it is necessary according to the Draft Guidance to establish the **specific form of the indicator** of a local nexus in the respective jurisdiction[33]. In the MWG's view, the Draft Guidance is over-broad and vague in some respects:

- The activity of a company shall be attributable to the place of intended use. While this shall usually be the place where the customer is located,[34] companies engaged in e-commerce may be dealing with customs located in a vast number of jurisdictions – and they may do so even without actively competing for business in these jurisdictions.

- The MWG strongly questions whether for research and development activities, it really should be relevant where these activities take place, (i.e. location of the staff as well as equipment and infrastructure)[35]. Where such activities concern an R&D market (i.e. contract R&D undertaken for third parties), the location of the customer for such services will be relevant. If the activities concern internal R&D that is preparatory for market facing activities, the location of the assets used for R&D are completely irrelevant. In a globalized economy, they could be anywhere; more importantly, for assessing the relevance for domestic competition, the location of the internally used assets is meaningless. They are internal by their very nature and thus do not provide any indication of where competitive effects of a transaction will occur. Thus, what does matter – but is ignored by the Draft Guidelines – is whether there is a direct link between R&D and at least potential products or services offered for the domestic market. It should be recognized that products are not necessarily developed to be marketed at the place of R&D. Activities that relate to an entry into the domestic market are only mentioned as a further possibility to establish the local nexus.

4.9 The domestic activity must be **market related**[36]. This requirement may be challenging to assess in situations where activities have not yet been monetized:

- Other consideration than payment may be relevant (e.g. users in the geography consume services (for which they may not pay a monetary compensation but deliver data as consideration) or advertisers direct advertising at a certain geographic region);

- Services are offered for free but monetized in a different way or payments intended at a later stages or (e.g. an app is initially used for free but paid content or advertisement later or in parallel, premium content);

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such, the reading of the explanatory notes needs to be narrowed to establishments with existing market orientated activities towards Austrian customers at the time of the filing (essentially in line with explanations of the Draft Guidance for Germany, see para 66 and 70).

[33] See para. 68 of the Draft Guidance.

[34] See para. 69 of the Draft Guidance.

[35] See para. 71 of the Draft Guidance.

[36] See para. 73 of the Draft Guidance.

- Market related R&D activities have to be distinguished from basic research. A determining factor according to the Draft Guidance is whether the research result will be marketable. It shall not be necessary that there is already turnover created or a product marketed. However, it cannot be sufficient that a laboratory in the US developing a product that may ultimately also be sold in Germany is already pursuing a domestic market related activity.

4.10 These categories may provide certain guidance. However, it is obvious that this cannot cover all potential future situations that may have to be assessed by the Agencies. It also raises many questions with regard to the determination of whether there is actually some sort of monetization in various constellations, (e.g. what kind of user data or which level of detail for such data is required to determine the market relation). This creates the risk that such criteria may lead to an overly broad definition of domestic activities. Therefore, the Draft Guidance should be more precise in this respect. It should be clarified if there is a quantitative minimum required for alternative ways of monetization and how the significance could be measured (i.e. quantity and quality of delivered customer data). Expected future monetarization may again lead to uncertainty as it relates to potentially intended future activities. For example, an app might not become as successful as expected or the future monetization might only happen several years from the date of notification.

4.11 With regard to R&D activities the Draft Guidance does not provide clear guidance regarding the minimum requirements as to the achieved level of product development and seems to overstretch the scope of market orientation. There may be cases in which developed products will only be marketable many years later or it might be very uncertain whether the product will be marketed at all. In this regard, the Draft Guidance does not offer administrable objective criteria, rather it claims to employ a quite flexible approach that may consider various factors. The Draft Guidance confuses actual domestic effects and potential future effects. The former are required to trigger the application of German law the latter may become relevant in the substantive assessment of a transaction. The MWG is concerned that this will lead to a high degree of legal uncertainty. As such, the MWG strongly advocates that the agencies should provide clear quantitative criteria for an administrable safe-harbor.

4.12 With regard to the **significance of the domestic activity**, the Draft Guidance does not provide much guidance. It is noted that the established law does not contain any quantitative criteria (cf. para. 78). But this does not preclude the Agencies adopting guidance that includes clear quantitative indicators; this is all the more important as the quantitative trigger for German merger control to apply (minimum turnover 5 million EUR) is disapplied in this context. It would thus be necessary to provide objective criteria that constitute the equivalent of this monetary threshold to provide the necessary clarity for purposes of applying this threshold.

4.13 The MWG suggests that the Draft Guidance currently fails to provide this; it again refers to domestic sales: If the current domestic turnover of target is below EUR 5m and adequately represents market position and potential, this will not be regarded as significant activity. However, the basis for using this criterion is whether the turnover below EUR 5m *"adequately reflects the market position"*. The latter is not a quantitative criterion, but a rather discretionary assessment. It remains unclear how the notifying parties will have sufficient certainty that the Agencies will agree that such an assessment is applicable. In the MWG's view, there should instead be a presumption that the domestic turnover of an existing product adequately reflects the market position unless the goods or services in question are usually offered for free. This should also apply in cases where paid premium content is only consumed by a small share of the local

users. Turnover created with third party payments for advertisement and the number of customers as potential addressees of advertisement might also be considered to trigger the presumption.

4.14 For Austria the Draft Guidance offers very little guidance on mergers in the "old economy", (i.e. industries where the turnover of an undertaking adequately reflects its market position and competitive potential). While the Austrian law does not mirror the approach taken in Germany (providing for a turnover-based carve-out threshold of EUR 5m in para. 79 Draft Guidance), the Committee encourages the BWB to provide further guidance on the significance of domestic activities. This is all the more important as the initial experience with the transaction value test has shown its wide reach outside the digital industries that were the intended focus of this extension to the merger control regime. As such, there is the potential to bring in a large number of mergers lacking appreciable domestic activities into the jurisdiction of the BWB. In line with the ICN's Recommended Practices,[37] the Committee would welcome an easily administrable safe-harbor based on quantitative criteria. This could preferably be turnover-based (in analogy to Germany). In the alternative, the BWB might consider introducing an appreciability threshold based on which activities of the target company measured by its market share on the domestic market would be indicative for the absence of significant activities (e.g. below 10% or 15%). [38]

4.15 The Agencies' approach to provide examples in the Draft Guidance is highly appreciated. However, some of these examples do not provide as much practical guidance as would be desirable:

4.15.1 The digital economy examples provided in para. 82 et seqq., indicate that 1 million app users in Germany shall apparently be sufficient to constitute significant domestic activity. From a methodological perspective it remains unclear whether it is decisive for the local nexus that (1) the app is marketed (also) to end users in the respective country or (2) whether a certain minimum amount of local users is specified. This must be distinguished from the question of whether the local nexus is sufficiently significant. Seemingly, as a quantitative indicator, the amount of users serves to show the significance of the domestic activity. However, it is not explained why is 1 million users – which only represents a tiny percentage of the population – regarded as "significant". The MWG suggests that the Draft Guidance establishes a clear safe haven in this regard with an assumption that anything less than 1 million users for an app should not be considered "significant". Also, the MWG suggests that a similar approach be applied for the frequency of access of a website by domestic customers – but that the numbers must be significantly increased to reflect usage patterns. More generally, it remains unclear whether the customer or user base needs to cover a certain percentage of overall consumers or users in Germany (or Austria); the MWG – making reference to ICN best practices – suggest that clear, objective, and easily established criteria be used to give shape to what might otherwise be a criterion that is hardly able to establish a proper jurisdictional criterion. The experiences that have led to the establishment of a second domestic turnover criterion should be applied in this context as well.

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[37] ICN Recommended Practices, Item II. E.

[38] The MWG would have a strong preference for a turnover-based approach, given that market share thresholds are not easily administrable: see ICN Recommended Practices, Item II. E., Comment 1.

4.15.2 Otherwise, this definition of domestic activities is likely to make many concentrations of internationally operating undertakings that have EUR 400m/200m transaction value subject to notification in Germany/Austria if no quantitative minimum amount for such activities is included to define an appropriate level of materiality. This would, however, contradict the well-established principles of jurisdiction of international law, notably the requirement of significant domestic effect, if proposed concentrations were subject to notification where the domestic relationship is limited to use by only a small number of cross-border customers. Therefore, the Draft Guidance should stipulate a minimum amount for the amount of (active) local customers or the frequency of access of a website by local customers.

4.15.3 The examples regarding the acquisition of a pharmaceutical ingredient (paras. 99 et seqq.) also raise further questions:

- The first example refers to the acquisition of a company that received approval for a certain drug in the EU and the US with a turnover in Germany below EUR 5m (EUR 1m in the first year and EUR 3m in the second year following approval). [39] The positive assumption of significant domestic activity is apparently entirely based on the fact that the domestic turnover shall not be adequate to reflect the "competitive potential". While the example excludes turnover, it does not positively define the applicable indicator in the case at hand. The presumption of an allegedly higher "competitive potential" is nothing other than expected or future aspects that – according to the Draft Guidance's own wording – should not be considered: "*Future or anticipated activities are not sufficient; this also applies to currently insignificant domestic activity that can be expected to reach a significant level in future*[40]". If most recent exponential growth is considered to <u>exclude</u> turnover as a criterion it is nevertheless to a certain extent considered within the vague term "competitive potential". Moreover, it is important to recognise that speculations with regard to "competitive potential" might not materialize. Besides the significant legal uncertainty the parties would also have incurred costs for the notification even though the business did not remain as successful as assumed at the time of the merger control assessment. Moreover, "competitive potential" is not a quantitative criterion that can be easily assessed by the notifying parties. Further clarification would be important if the Agencies maintain this criterion.

- The second example concerns drug development: The target has a research site in Germany. It is stated that "*[t]he fact that the buyer is prepared to pay € 400m is an indication of significant domestic activity in Germany*".[41] In this case, the Draft Guidance refers to the value of the transaction to indicate significant domestic activity and to the fact that the drug has just entered phase II of clinical trials. However, this may not be appropriate as the value of the transaction may reflect the worldwide potential of the drug and in principle is not appropriate for

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[39] See para. 100 of the Draft Guidance.

[40] See para. 67 of the Draft Guidance.

[41] See para. 102 of the Draft Guidance.

assessing a possible local nexus. Moreover, in the provided example, a small research budget and a small amount of researchers shall not prevent the assumption of significant domestic activity. Again, no clear minimum requirements have been identified for domestic research and development activities. Moreover, phase II is quite far from the actual ability to market a product and therefore is still subject to a very high degree of uncertainty. The Committee encourages the Agencies to consider whether phase III should be regarded as the pre-requisite for considering notifications related to potential drug products.

4.16 In summary, the MWG's view is that the Draft Guidance does not yet provide a sufficiently, objective, clear, and material standard with regard to the local nexus that is appropriate for implementation of the substantial domestic operations requirement. The fact that the domestic turnover of the target is nevertheless considered "*if this turnover adequately reflects its market position*"[42] shows that in some situations there is seemingly no real alternative to assess domestic effects even in cases under Section 35 (1a) GWB. Quantitative criteria without any minimum amounts provided (e.g. local user base, R&D budget, etc.) or mere qualitative criteria (e.g. "competitive potential" or "adequate reflection of the market position") will not provide sufficient legal certainty for the notifying parties. It is very likely that such criteria will lead to different conclusions and to the necessity of a constant dialogue between the notifying parties and the Agencies. This will increase costs and workload for both the parties and the Agencies as well as fostering uncertainty that has a negative impact on the acceptance of German and Austrian merger control rules overall.

5. CONCENTRATIONS

5.1 The Draft Guidance correctly states that, following the 9th amendment to the GWB, the requirement that the buyer be put into a position of being able to join an existing market position of the seller can no longer be maintained unreservedly[43]. In accordance with the 9th amendment to the GWB, it will no longer be possible to insist that the part of the asset to be acquired is the basis of a *current* market position. The new provisions merely state that a concentration may occur even if the target has not achieved any turnover. It does not dispense with the requirement that a market position is taken over. Where there is only a prospect of future activities, an assets is taken over, not an undertaking. The Draft Guidance apparently confuses the existence of a market related activity and the generation of turnover. The fundamental principle of legal certainty requires that the Draft Guidance should be more precise and narrow as to when the buyer's *future* market position can be influenced. In the MWG's view, there must be a clearly defined quantitative criteria for the circumstances under which assets form the basis of a future market position.

5.2 Traditional thinking in horizontal mergers is based on the fact that one company acquires its competitor (which may or may not have negative implications for competition – but that is a substantive question). The commercial situation here has been that two companies build a business and corresponding market positions geared towards competing for sales of the relevant products or services on a lasting basis and at some stage one takes over the other. The Draft

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[42] See para. 79 of the Draft Guidance.

[43] See para. 108 of the Draft Guidance.

Guidance extends this to start-up companies or pure R&D activities. Here, the business rationale is completely different: Start-ups or R&D activities are not set up to win the market – they are usually set-up to develop a new product/service and then be sold as soon as the viability of the product/service is established. Usual acquirers are companies who have resources and interest to grow the opportunity. The involved companies are active on a market that is separate from the market for the relevant product. They are active on an upstream service market and the assessment should acknowledge this. The "classic" test has been something like "I buy a very expensive paper machine, can this be a concentration?" To which the answer was "Yes, if there is a market position attached to it.

5.3 Regarding the existence of a "concentration" it needs to be clear that merger control – which focusses on changes to the structure of competition – still requires a transfer of a market position. Simply buying assets – whether it is a machine, a patent, an app, or hiring a couple of specialized employees – which simply allows the buyer to develop a competitive position should not be sufficient to trigger merger control. If the scope of merger control was extended to any acquisition of useful assets, this would overstretch the scope of merger control significantly.

5.4 From a competition policy perspective, the implications of interfering with outsourced product development and R&D need to be carefully considered. Such interference by way of merger control might hurt innovation and competition rather than preserving it.

5.5 When undertakings are considering entering a new market or country, they generally do not, in the experience of MWG members, plan further ahead than for two or three years, and even then there may be significant uncertainty as to whether plans are likely to be implemented. These uncertainties tend to be even greater in the dynamic digital economic sector which is the primary impetus for the proposed new thresholds.

5.6 The MWG suggests that an assessment regarding future domestic activities for purposes of establishing the relevant local nexus (not whether a concentration occurs) should be based on a combination of both (i) existing market related activities (even if they do not generate any turnover) and (ii) the German turnover an undertaking is expected to have after a period of two or three years at most. In the MWG's view, the prerequisite for such a notification obligation could be an annual turnover in excess of EUR 5 million which the undertaking in question aims to achieve within two or three years. This would be in line with the established second domestic turnover threshold.[44] A specified level of assets within Germany is another possible approach.[45] Alternatively, a threshold tailored specifically to the digital economy could be based on some established level of user accounts (e.g. 1 million active accounts within an expected three year time frame).

5.7 The Austrian legislator did not provide for a provision in the KartG comparable to Section 18 no. 2a GWB, as amended. Thus, the introduction of the transaction value test in the KartG did not go along with a widening of the concept of concentrations in Austria. As such, the proposal of the Draft Guidance in para. 111, which alludes to a similar reading of the now widened approach in Germany is questionable. Indeed, Austrian law requires the acquirer to assume an existing market

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[44] Section 35(1) no. 2 GWB.

[45] As noted above, the United States use either assets or sales to establish its local nexus requirements.

position of the seller in order to constitute a concentration subject to merger control[46]. Therefore, the mere potential to influence the future position of the acquirer is – unlike Germany – not sufficient to qualify as a concentration under the Austrian merger control provisions.[47] Hence, transactions where the buyer would have to take further steps to develop the acquired product / product know-how before being able to start its distribution, cannot be regarded as concentrations under Austrian law. The Committee encourages the BWB to confirm this point in the final guidance paper.

5.8 In the same vein, the BWB might clarify the application of the transaction value test to the formation of a new joint venture in Austria[48]. In Austria, the creation of (non-full function) greenfield joint ventures (i.e. a non-full function joint venture where the parties do not contribute and/or acquire an existing business), does not amount to a concentration. It would be useful to confirm this point in the final guidance paper as well.

6. CONCLUSIONS

6.1 The MWG welcomes the Agencies' willingness to provide guidance and case studies. It goes without saying that guidelines cannot cover all scenarios or deal with every possible industry and activity in extensive detail. Nevertheless, remaining legal uncertainties should be minimized where possible. Many criteria discussed in the Draft Guidance do not provide the objective "bright lines" that are recognized to be important in the ICN Recommended Practices.

6.2 When assessing the proposed new merger control thresholds, it should be borne in mind that German and Austrian law stipulates very high administrative fines in case of completion of a concentration that is subject to notification but is not cleared by the BKartASuch behaviour is prohibited and punishable by a fine of up to 10% of the undertaking's worldwide annual group turnover.[49] If in doubt, therefore, undertakings will tend to make a notification in Germany and Austria, particularly if the notification requirement remains vague despite considering the guidance issued by the Agencies. This would lead to the notification of concentrations that have no appreciable domestic effect, which presumably is not the intent of the legislators or the Agencies. Notifications will mean significant extra costs for the notifying parties, not to mention the time and resources involved for the BKartA and the BWB.

6.3 That apart, the creation of an overly broad notification practice would harm Germany's and Austria's credibility in the international economic and competition policy communities. In the Committee's respectful opinion, some of the proposed criteria in the Draft Guidance do not comply with the local nexus and objectivity principles that are internationally recognized as best practices for merger control.

6.4 In particular, German antitrust practice has often been a role model for foreign competition authorities and foreign legislation in competition matters. Should the new Section 35(1a) GWB

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[46] See para. 110 of the Draft Guidance.

[47] See para. 108 of the Draft Guidance.

[48] See para. 52 of the Draft Guidance.

[49] Section 41(1) sentence 1 GWB, Section 81(2) no. 1 in conjunction with Section 81 (4) sentence 2 GWB; Section 29(1) lit. a KartG.

(and Section 9 (4) KartG) become a model for other jurisdictions as well, this would place German and other multinational undertakings in the unfortunate position of being required to notify transactions in numerous jurisdictions which have little or no nexus to them. This would not be in the best interest of the German economy and would not represent sound domestic or international economy.

6.5 In light of the above, it will be important that the Agencies provide statistics with regard to actual experience under the transaction value thresholds and consider updating their guidelines and/or issue case notes to address remaining uncertainties.

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