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Insights

SAFETY NET OR OVERREACH? THE EUROPEAN COMMISSION'S NEW POLICY ON MEMBER STATE MERGER REFERRALS

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SUMMARY

In 2020, European Competition Commissioner Margrethe Vestager announced a new policy, under which the Commission will entertain requests from Member States to review mergers that do not meet the notification thresholds for the EU or in any Member State. This policy has now taken effect – with at least one transaction already being considered for referral, and the Commission releasing a guidance document on the new policy.

On the face of it, the new policy may not seem like much of a change. Indeed, the EU Merger Regulation has always allowed such referrals. However, to date, the policy of the Commission has been to only accept referral requests for deals that were notified in a Member State. By changing their policy, and being willing to accept (and encourage) requests for deals that are otherwise not notifiable, the Commission is inevitably bringing a significant degree of regulatory uncertainty to many deals and dealmakers.

The Perceived Problem

Under EU law, if a merger is notifiable to the European Commission under the EU Merger Regulation, it cannot be reviewed by any Member States. If it is not notifiable to the European Commission, then merging parties need to check whether it may be notifiable in one or more Member States. By confirming whether the notification thresholds at EU or Member State level are satisfied, merging parties are provided (with a few limited exceptions) with certainty as to whether their deal requires notification and review by a competition agency.

There are, however, a number of exceptions to this EU "one stop shop" rule, which allow deals to be referred from the Commission to Member States and vice versa. One such provision is Article 22 of the EU Merger Regulation, which allows one or more EU Member States to request that the Commission review a deal. As noted, historically, the Commission's approach has been to only

accept such requests if the transaction met the merger notification thresholds in one or more Member States, which has resulted in this provision being used rarely – less than 0.5% of mergers examined by the Commission have been referrals under Article 22.

Over recent years, however, the Commission and other agencies worldwide have expressed concerns that, given notification thresholds are most often based on revenue figures, a number of so-called "killer acquisitions" may slip through the merger control net. These are deals where a start-up target (most often in the technology or pharmaceutical space) is not yet generating sufficient revenue to satisfy turnover thresholds, but has the potential to become a significant competitor on the market – so-called "low-revenue/high-value" targets.

Having considered various ways to capture such transactions (such as notification thresholds based on transaction value – as have been implemented in Germany and Austria), in 2020 EU Commissioner Vestsager announced that a solution was "hiding in plain sight" – Article 22. The Commission announced that it would now accept referral requests under Article 22 for transactions that did not meet notification thresholds in any Member State.

The Commission Guidance

Unsurprisingly, the Commission's announcement caused concern amongst competition lawyers and businesses. Dealmakers could find themselves in a situation where, having determined that notification thresholds were not met at EU level or in any Member State, the Commission nevertheless reels in their transaction for review via Article 22. This would leave many deals with a residual uncertainty that could not easily be resolved. The Commission's promised guidance on the application of Article 22 was, therefore, much anticipated.

The Commission's guidance document was released on 26 March 2021. It will, no doubt, go some of the way to reducing the concerns of the business community. Most importantly, the guidance is clear that the most appropriate cases for referrals where a deal is not otherwise notifiable would be transactions *"where the turnover of at least one of the undertakings concerned does not reflect its actual or future competitive potential".* More specifically, the guidance goes on to note that this could include cases where the undertaking in question:

- is a start-up or recent entrant with significant competitive potential that has yet to develop or fully implement a business model generating significant revenues;
- is an important innovator or is conducting potentially important research;
- is an actual or potential important competitive force;
- has access to competitively significant assets (such as for instance raw materials, infrastructure, data or intellectual property rights); and/or
- provides products or services that are key inputs/components for other industries.

In addition, it's important to note that referrals under Article 22 can only be made if the transaction threatens to affect trade between EU Member States and threatens to significantly affect competition within the Member State or Member States making the request.

What does this mean for dealmakers?

There are a few key points that dealmakers should be aware of now that this new policy is coming into effect:

- **A new uncertainty:** Notwithstanding the guidance, the Commission retains significant discretion in deciding which referral requests to accept or press for, and it is clear that the examples in the guidance are illustrative only and the mechanism is not limited to any sector or sectors. As such, the Commission may be willing to entertain referral requests that go beyond the examples listed in the guidance. Commission officials have also commented that the early days of this policy will be in effect a "testing phase", giving the Commission an opportunity to determine how effective and workable the new policy is and whether changes and new guidance will be needed in light of practice. So, it may be that they don't anticipate too many deals being referred in the near future. Inevitably, though, parties doing deals across Europe will be faced with a new degree of uncertainty not previously part of EU practice – particularly in the early days of this new policy.

- **But it's not all bad news:** Despite this new uncertainty, the risk of referrals for the majority of transactions (in particular those that do not raise significant competition concerns) should remain very low.

- **Case-specific guidance possible:** Positively, Commission officials have suggested that they will be willing to offer informal guidance to merger parties as to whether their deals may be candidates for a referral. This will help provide a degree of certainty to parties involved in deals that may raise cross-border competition issues but are otherwise not notifiable. However, the Commission would not provide a "definitive" view and merger parties may have no choice but to go ahead with the deal and accept the residual risk of a possible referral – which could even happen after completion.

The new policy has already shown signs of use too, with the French Competition Authority sending a referral request to the Commission in March in relation to a deal in the health technology space – a deal that did not meet the French notification threshold. The parties have – unsuccessfully – challenged the referral request before the French courts, but it remains to be seen yet whether the Commission will accept the request, or whether there will be further legal challenges.

Conclusion

Commission officials claimed that the new policy is simply a "safety net", and not an "indiscriminate catch all". Such comments, along with the Commission's guidance, should provide

some degree of comfort to businesses and their advisers. That said, particularly during the early days of this policy, businesses engaging in deals may continue to face a significant degree of uncertainty, and it remains to be seen whether the possible benefit outweighs the high degree of uncertainty that it will lead to for businesses – particularly given the existing referral mechanisms and policies have already seen the Commission review technology deals it may otherwise have missed.

The coming months and years will show how aggressive Member States and the Commission will be in this regard, and it is to be hoped that these powers are used rarely and wisely. We also hope (and advocate) that, as the Commission's practice under this policy develops, its guidance will be updated to reflect its experiences and approaches as the policy matures. This would, hopefully, over time allow businesses and their advisors to have a greater degree of certainty as they embark on new transactions.

BCLP's Antitrust & Competition team is involved with the Commission and Member States with regard to this new policy and will continue to advocate for more certainty and clarity as it develops in practice. If you have any questions about the content of this article, or EU merger control more generally, then don't hesitate to get in contact with any of the lawyers listed.

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