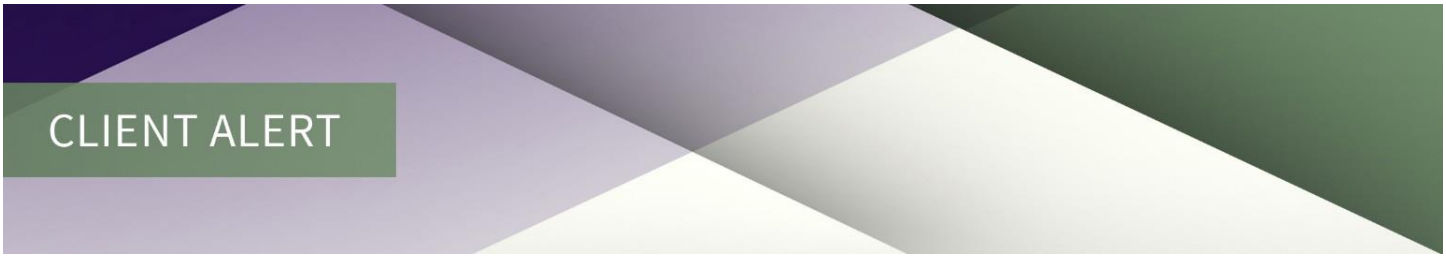

Wolf in Sheep's Clothing: European Commission's New Policy on Case Referrals Creates a *De Facto* New Filing Requirement for Deals Below Merger Control Thresholds

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On 26 March 2021, the European Commission (the "Commission") published new guidance on how it will apply referrals of merger control reviews from EU Member States "upwards" to the Commission ("Upward Referral Guidance"). What sounds like a communication on a technical procedural issue may have a dramatic impact on deal execution for many transactions. The Upward Referral Guidance creates a new process to allow the Commission to review transactions which neither trigger a one-stop filing obligation with the Commission under the EU Merger Regulation ("EUMR") nor are notifiable to any competition authorities at EU Member State level under their domestic merger control regimes. This change should in particular impact acquisitions of small innovative companies by bigger players, especially in (but not limited to) the digital, biotech, and pharma sectors, e.g. as a means for the authorities to better scrutinize so-called "killer-acquisitions".

The Commission introduces these sweeping changes not through new legislation (with new filing thresholds) but through a mere change in its policy in relation to the existing case referral mechanism set out in Article 22 EUMR.

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Background: The Article 22 EUMR referral regime and the Commission's practice to date

Under Article 22 EUMR, a Member State or several States (in practice, their national competition authority – "NCA") may request the Commission to examine a concentration that does not meet the thresholds under the EUMR for a one-stop shop merger review but (i) "*affects trade between Member States*" and (ii) "*threatens to significantly affect competition within*" the requesting Member State/s. This referral mechanism, also referred to as the "Dutch Clause", was introduced in the original EUMR in 1989 to allow Member States without a national merger control regime (such as the Netherlands at that time) to ensure that potentially anticompetitive mergers could be reviewed at least by the Commission. This is precisely the door opener for the sweeping effects of the Commission's new Upward Referral Guidance: Article 22 EUMR does not require that a deal is notifiable under the domestic regime of the requesting Member State/s. However, up until now, the Commission applied a policy of discouraging referral requests under Article 22 from NCAs that do not have jurisdiction under their domestic regime to review a transaction because, based on the Commission's experience so far, such transactions "*were not generally likely to have a significant impact on the internal market*".[1]

The Commission's shift of policy

This policy has now changed. Executive Vice-President Margrethe Vestager, in charge of the Commission's competition policy, said a *"number of transactions involving companies with low turnover, but high competitive potential in the internal market are not reviewed by either the Commission or the Member States."*[2] Noting further that a *"more frequent use of the existing tool of referrals under Article 22 of the Merger Regulation can help us capture concentrations which may have a significant impact on competition in the internal market."*[3] She announced in September 2020 that the Commission would "*start accepting referrals from the national competition authorities of mergers that are worth reviewing at the EU level – **whether or not** those authorities had the power to review the case themselves*" (emphasis added).[4]

Now, with the Upward Referral Guidance, the Commission officially encourages NCAs to consider making Article 22 referral requests to the Commission ***even if*** the referring NCA(s) do(es) not have jurisdiction to review the transaction under its/their national merger control regimes. The main elements of the Upward Referral Guidance can be summarized as follows:

- ***New criteria for the identification of potential candidates for referrals*.** Besides the formal requirements contained in Article 22 EUMR itself, the Commission considers that referrals will be appropriate in cases where

1 Article 22 Guidance, para 8.

2 https://ec.europa.eu/commission/presscorner/detail/en/ip_21_1384

3 Ibid.

4 Margrethe Vestager's Speech, "*The future of EU merger control*", International Bar Association 24th Annual Competition Conference, 11 September 2021.

the turnover of one undertaking (usually the target) is not reflective of its actual or future competitive potential.[5] The Commission identifies in its guidance the following *illustrative* situations). The target:

- is a start-up or recent entrant with significant competitive potential that has yet to develop or implement a business model generating significant revenues (or is still in the initial phase of implementing such business model);
- 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 its assessment, the Commission may also take into account whether the purchase price is particularly high compared to the current turnover of the target.

- ***The Commission will accept referrals even if the transaction has already closed*.** However, the Commission indicates that it would generally not accept a referral where more than six months have passed after closing, provided that the implementation of the deal was in the public domain, e.g. as a result of a public announcement of the closing of the transaction. Otherwise, the six-months period will run as from the date the material facts of the transaction have been made public. In any event, the six-months period is only indicative and the Commission expressly reserves its right to accept referral requests to review transactions under the Article 22 mechanism even after this time period has elapsed.

Key practical implications: Less legal certainty, time consuming procedure

Although it is anticipated that mainly platform, tech and pharma deals will be the subject of Article 22 referrals by Member States which do not have jurisdiction to review the transaction, as a matter of policy any merger involving a competitively sensitive transaction – irrespective of transaction value and target revenues – could be caught by this policy change.

So far, falling below the thresholds of the EUMR and of Members State regimes was sufficient to exclude a merger review. Also, often, if only one (or very few) NCA(s) had jurisdiction to review the transaction, the risk of an upward

[5] A similar concept as outlined in the Upward Referral Guidance is used in the context of the consideration value-based thresholds that were introduced into German and Austrian merger control in 2018 and explained in the two authorities' joint guidance.

referral was manageable, for example, because the authority/ies did not have any track record of making such referral requests.

Under the new policy, companies and their advisors need to quantify the risks of a review of the deal by the Commission triggered by an Article 22 EUMR referral from an NCA, either on initiative of the NCA or upon invitation by the Commission, even in cases where the transaction is not notifiable at all anywhere in the EU, either at national or at Commission level. This has the potential to significantly increase execution risks and creates unwelcome legal uncertainty.

While in many cases the risk of a referral will in practice remain low because of clear indications that the transaction will not threaten to significantly impede competition, irrespective of the likely frame of reference adopted, it will be important to identify those transactions which are at greater risk of such referrals. In particular in relation to such transactions which are at greater risk of referrals, parties need to consider whether to consult the Commission or relevant national competition authorities on the prospects of referral requests being made by national competition authorities and being solicited and/or accepted by the Commission.

Should a deal cause the Commission to invite and/or NCAs to initiate a referral request, it will take a significant amount of time until the outcome is clear. This is because a referral request initiates a consultation process between the Commission, the requesting NCA, and all other EU NCAs under set deadlines that, in total, may take several months until the actual merger control review before the Commission can be initiated or it is clear that the deal will not be referred. Obviously, this will have a significant impact on deal planning and execution and should be factored in from the very beginning when a candidate deal kicks off.

The power to pick up deals post-closing causes the biggest concerns within the M&A community and raises fundamental legal questions as to the Commission's power under the EUMR and the Treaty for the Functioning of the European Union. Some comfort maybe be taken from the statement of the head of Directorate Competition, Olivier Guersent, at a recent webinar that companies must not worry that their deals could be reviewed for an indefinite period of time after closing.[6] Comfort that merger control rules will be applied proportionally may be taken from the Commission's roadmap published in parallel to the Upward Referral Notice on simplifying merger rules under plans put out for public consultation, allowing enforcers to concentrate on cases most likely to impact competition while streamlining the process for unproblematic deals.

But, overall, the regulatory environment for mergers in Europe, where the UK has dropped out of the one-stop-shop principle under the EUMR, appears to becoming more complex and professional deal planning will be an ever more important factor for getting deals done swiftly.

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[6] Webinar on Article 22 referrals organized by the French competition authority on 23 March 2021.

If you have any questions regarding this client alert, please contact the following attorneys or the Willkie attorney with whom you regularly work.

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