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Germany Proposes Transaction Value Threshold to Require Notification of High Value Deals Even with No/De Minimis Sales in Germany

Werner Berg (Baker McKenzie) · Friday, July 22nd, 2016

With little fanfare, on Friday, 1 July 2016, among a raft of other amendments to the Act against Restraint of Competition ('ARC'; 9th amendment), the Federal Ministry of Economics proposed a far reaching change to German merger notification thresholds making it one of the few jurisdictions worldwide that take jurisdiction based on the size of the transaction, no matter how trivial the sales of the target are in Germany.

The policy intention was explicitly to bring into the Bundeskartellamt's net major deals – struck anywhere in the world – with a high value target whose potential in sales is as yet unrealized. This will often be the case with innovative IT- or life-science targets, or those controlling key technologies, whose innovations have not yet come to market. The Facebook/WhatsApp acquisition is given as a prime example of the kinds of deals where the German authorities would like to take jurisdiction.

The draft foresees the implementation of a filing threshold that would be triggered if the consideration paid by the acquirer were to exceed € 350 million. This proposal and its practical implications will be introduced in more detail below.

The current draft[1] has been produced in close cooperation with the German Federal Ministry of Justice and in consultation with the Bundeskartellamt. It has to be approved by the German government and will afterwards be presented to the German parliament, which will very likely make a number of modifications to the draft. Since the draft law also takes care of the transposition of the Damages Directive which has to occur by 27 December 2016, it is expected that the law will still enter into force this year.

The current thresholds

Concentrations have to be notified in Germany if all undertakings together generated € 500 million of turnover worldwide in the last financial year and one undertaking has generated € 25 million in Germany and another undertaking has generated € 5 million in Germany in the last financial year.

There are two exceptions to this: First, even where parties to a concentration reach these thresholds, they are not subject to merger control if the target is an independent undertaking that had less than € 10 million turnover in the last business year (so-called *de minimis clause*). This rule

is intended to make it easier for small undertakings to give up their independence and affiliate with a larger undertaking and the exemption from merger control is justified because the concentration is deemed not to have macroeconomic importance.

Substantive merger control does not apply, either, if the market affected is a so-called *de minimis market* (so-called 'minor market clause'). This is the case if the market concerned is one in which goods or commercial services have been offered for at least five years and which had a sales volume of less than € 15 million in the last calendar year. The rationale behind this provision is that those markets which are not relevant in relation to the economy as a whole are excluded from merger control. By demanding that the market has to have been existent for at least five years, mergers on newly developed and still expanding markets are caught by the provisions on merger control. The calculation for the purpose of the minor market clause has to be made for with regard to the turnover in Germany, not with regard to a possibly wider geographical market; this is because the purpose of the clause is to exempt markets from merger control which are of minor importance relative to the domestic economy.

The new threshold

The proposal now suggests that for deals where the second domestic threshold of € 5 million is not triggered, a notification is still required if the price for the target exceeds € 350 million and at least one of the 'other undertakings' (i.e. not the one that achieved the € 25 million in Germany) is active or will presumably be active in Germany. The motivation for this amendment is to capture transactions which have a macroeconomic importance with a local nexus but fall below the current thresholds. The Minister refers to the acquisition of WhatsApp by Facebook which was captured neither by German nor, initially, by EU Merger Control despite a purchase price of approximately US$ 19 billion. The matter ultimately came to the European Commission through referral initiated by Facebook from three other Member States.

None of the two exceptions shall be applicable if the new threshold is triggered. The *de minimis clause* is not applicable because the reason for the new threshold is exactly the presumed macroeconomic importance of the transactions triggering it. The limited size of the target can therefore not trigger a presumption to the contrary.

Neither is the minor market exception applicable. Again, the rationale for the exception does not fit because the assumption behind the new threshold is that the transactions triggering this threshold are in fact important in relation to the German economy as a whole. In this context, it is worthy of note that the draft clarifies that unpaid services may constitute markets.[2]

The consideration and its calculation

The draft law refers to the value of the consideration for the concentration. This resembles the size of transaction test in the US. The consideration encompasses all assets and other monetary values which the vendor receives in return for the concentration and also includes the value of financial liabilities which the acquirer may accept as part of the transaction. It does not matter whether the assets or monetary values are located inside or outside Germany, the global consideration is relevant.

It is argued in the motivation for the draft law that the € 350 million threshold ensures that only cases are captured which are economically important. But the authors of the draft law recognize

that no official statistics or other reliable bases are available to set a threshold at the right level. This is also due to the fact that purchase prices are considered business secrets and did not have to be reported to the Bundeskartellamt or otherwise[3] so far. According to the authors, research revealed that in 2015 only in one transaction in Germany a consideration of € 350 million or more has been paid. Similar statistics apply for 2013 and 2014. The second German Federal competition authority, the Monopolies Commission, an advisory body to the German Government, on the other hand, had suggested to apply a similar threshold which would be triggered if the value added by the target were € 500 million or more.[4]

The local nexus

The new threshold will be triggered if one company has generated € 25 million of turnover in Germany in the preceding financial year and – and this is the new part – at least one of the 'other undertakings' (i.e. not the one that achieved the € 25 million in Germany) is active or will presumably be active in Germany. This test will create uncertainty for companies and their advisers. The draft law as such is silent on the criteria to be applied for when a company will 'presumably be active in Germany'. It does not seem, however, that a link to the value of the deal attributable to Germany (i.e. based on a pro-rated valuation of assets or revenues) is required under the current draft. The motivation refers to users/customers served and to R&D activities undertaken in Germany. Whilst the activity needs to be 'market-related' it is not necessary that it is paid for. Importantly, the motivation explains that the time horizon for the assessment of the potential activity in Germany is three to five years, which is in line with the general forecasting horizon under German merger control.

It is obvious that this provision and the interpretation suggested by the Federal Ministry of Economic Affairs will create uncertainties which will normally push the undertakings concerned towards filing. And if the parties to a transaction that would trigger (only) the new threshold were initially certain that there will no other undertaking be presumably active in Germany, what would it mean, if they decided to become active in Germany with the acquired business two years later? At the time when the concentration was closed, the other undertaking was not 'presumed to become active in Germany'. There is thus no need to file, not even two years later when the change of mind occurs. But will the Bundeskartellamt believe this if and when they investigate the matter? The parties would be well advised to keep as much documentation on their objective plans until approximately five years from closing. Unless the legislator were prepared to establish local nexus criteria which are clear at the time when the transaction is undertaken, it might be easier and certainly less risky to file such transaction irrespective of the initial local nexus.

The information requirements, notably in the notification

According to the draft law, the notifying party has to provide the Bundeskartellamt, in the notification, with the value of the consideration and the basis for its calculation as well as with 'information as to kind and scope of domestic activities'. The Bundeskartellamt, on its part, will be entitled to ask for additional information about domestic activities including number and location of customers as well as places where its services are offered and used, respectively.

Impact assessment

On the basis of very limited statistical information as explained above, the Federal Ministry of Economic Affairs expects three additional filings per year as a consequence of the introduction of

the additional threshold, of which one case would be treated in the main proceedings, i.e. the so-called second phase. A first analysis of the new threshold with companies active in the IT space and additional research, notably in the pharmaceutical field, suggest that the number of additional filings is rather in the order of 15 matters, i.e. five times the expected amount. Much will depend on how clear the local nexus requirement will be formulated. Whilst it seems likely that pure German deals triggering that threshold are indeed rare, transactions that are primarily non-German seem much more frequent and could, absent clear local nexus rules, be captured by the new threshold, probably without sufficient justification.

Scope for changes of the draft; evaluation after three years

It is very likely that the new merger control threshold will be introduced into the German merger control rules. This is underlined by the fact that the Monopolies Commission made a similar suggestion in its Special Report 'The challenge of digital markets' in 2015.[5] The question is, however, whether the value amount remains at € 350 million or might be increased to, e.g., € 500 million as suggested by the Monopolies Commission. Another question is, whether the local nexus requirement could not be defined more clearly in order to allow the companies concerned and their advisers to make reliable assessments of the filing requirements before the transaction is implemented. In any event, it is foreseen in the current draft that the new threshold and the provision determining the value calculation shall be evaluated three after their entry into force.

This post was updated by the Kluwer Competition Law Blog Post of 8 November 2016 entitled "Government Proposal Amends Local Nexus Requirement for New Transaction Value Threshold – Update"

References[+]

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