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Bulgaria: Merger control decision annulled for turnover miscalculation

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The Bulgarian Supreme Administrative Court (“**SAC**”) in a 5-member panel (acting as final instance) has annulled the decision of the 3-member panel of the SAC (acting as second instance) regarding the appeal of a decision of the Bulgarian Commission for Protection of Competition (“**BCPC**”). The ground for annulment is the lack of analysis of the acquisition of Dunarit JSC by EMKO Ltd., and miscalculation of the turnover of the two companies – both major producers and traders with defence-related products on the territory of the Republic of Bulgaria.

Background

In 2016, BCPC was notified by EMKO Ltd. for its intention to acquire direct and sole control over Dunarit JSC by means of purchasing newly issued shares of the company’s capital (the “**Notification**”). Both companies operate on the market of the manufacturing, repair and trade of defence-related products.

EMKO Ltd. is solely owned by a natural person and does not control directly or indirectly any other undertakings, whereas Dunarit JSC forms part of a group of companies, whose beneficial owner has never been disclosed. Within the media there were rumours that the company was acquired and financed by Mr. Tsvetan Vasilev – the former majority shareholder and chairman of the Supervisory Board of the now declared insolvent Bulgarian Corporate Commercial Bank (“**CCB**”). So far, this information has never been confirmed and proven.

Dunarit JSC has two subsidiaries and is directly controlled by the Bulgarian incorporated Kemira Ltd., and indirectly by the Bulgarian incorporated Hedge Investment Bulgaria JSC and the Virgin Islands based EFV International Financial Ventures Ltd. (the off-shore company alleged to have as beneficial owner Mr. Tsvetan Vasilev).

A fact to mention is that Dunarit JSC is one of the largest military factories in the Republic of Bulgaria, financed by CCB as of its privatization in 2005. After the collapse of CCB in 2015, disputes for the control over the direct shareholder of Dunarit JSC – Kemira Ltd. began and several attempts to sell the company followed. In late 2015, Dunarit JSC’s management reached Mr. Emilian Gebrev (sole capital owner of EMKO Ltd.) with a request for financial support. In 2016,

EMKO Ltd., being itself one of the companies making the most of the trade in defence-related products, notified BCPC of its intention to acquire approximately 88% of the capital of Dunarit JSC.

On the Notification date, however, 91% of the capital of Kemira Ltd. was acquired by TMN Ltd.[1] As a result, Dunarit JSC became under the indirect control of TMN Ltd. and the natural person – Mr. Asen Babanski.

Initially, BCPC refused to commence the merger control proceedings for the review of the notified transaction[2] due to pending civil court proceedings resolving the legitimacy of the acquisition of Kemira Ltd. by TMN Ltd. Subsequently, this ruling was revoked[3] by the SAC and the merger control proceedings at issue were resumed.

With its decision BCPC found that the notified transaction did not constitute a concentration by means of Art. 24, para. 1 of the Bulgarian Competition Protection Act (“BCPA”) and therefore was not subject to mandatory clearance.

Applicable criteria and the BCPC decision

Under the BCPA, the acquirer is obliged to notify a transaction if the transaction results in change of control in the target and the following thresholds for turnover are met:

the sum of the total turnovers of all undertakings participating in the concentration on the territory of the Republic of Bulgaria for the previous financial year exceeds BGN 25 million; **and** one of the following:

- the turnover of each of at least two of the undertakings participating in the concentration on the territory of the Republic of Bulgaria for the previous financial year exceeds BGN 3 million

or

- the turnover of the undertaking which is the object of acquisition on the territory of the Republic of Bulgaria for the previous financial year exceeds BGN 3 million.

Additionally, Art. 25 of the BCPA provides for the general rule that the amounts to be included in the calculation of turnover should correspond to the ordinary activities of the undertakings concerned. The turnover calculation includes revenue from sales of any activity of the undertakings concerned, and not only the revenues realized on the market where the transaction will have an impact and the effective competition occur.

Therefore, pursuant to Arts. 24 and 25 of the BCPA and pursuant to its Methodology[4] the BCPC should have included in its turnover calculation the revenue from sales of the ordinary activities of the undertakings concerned, realised on the territory of the Republic of Bulgaria, excluded the proceeds from sales realised between the undertakings of the same economic group.

However, considering that the acquirer and the target mainly trade with their products abroad and

there the effective competition takes place, BCPC, contrary to the above rule, did not include the turnovers realised by the merging undertakings on the territory of the Republic of Bulgaria.

Appeal and court review

The BCPC decision was subject to appeal before the SAC by Viafot Investment Bulgaria Ltd. – a third party, claiming infringement of its interests. The third party refers to existing agreements for transfer of receivables against Dunarit JSC signed between E. Miroglio JSC and Viafot Investment Bulgaria Ltd., and subsequently between Viafot Investment Bulgaria Ltd. and Viafot Limited. Based on these agreements, for the third party rises the legal interest to challenge the BCPC decision, since the latter makes Viafot Investment Bulgaria Ltd. liable before the transferee of the receivables for the solvency of Dunarit JSC after the Notification.

The complainant, *inter alia*, challenges the analysis of the relevant product and the geographic market. According to the complainant, the aggregate turnover of the participants in the concentration is unlawfully calculated at less than BGN 25 million, where the financial statements of the acquirer and the target reveal amounts significantly above this number.

Viafot Investment Bulgaria Ltd. also objects the exclusion of undertakings concerned, namely those forming part of the economic group of Dunarit JSC and the lack of analysis on the impact of the concentration on the relevant market. Viafot Investment Bulgaria Ltd. claims that concentration between Dunarit JSC and EMKO Ltd. would negatively affect the competition on the market of manufacture and trade with defence-related products and would create monopoly. Nevertheless, the SAC acting as second instance in 3-member panel confirmed the challenged decision of the BCPC.

SAC's decision was then appealed before the final (cassation) instance – 5-member panel of the SAC. This panel of the court annulled the challenged decisions, finding that the turnovers of the undertakings concerned are indeed miscalculated – BCPC did not take into account the turnover realised on the territory of the Republic of Bulgaria and the undertakings concerned – the subsidiaries of Dunarit JSC, which are also subject to acquisition, given the indirect control exercised over them, were not included into the analysis and assessment of turnovers as part of the economic group. Additionally, the BCPC decision lacks any analysis on the circumstances related to the change in the control of Dunarit JSC and the expected impact of the notified transaction on the relevant market and the customers.

The case file was sent back to the BCPC with binding instructions regarding the calculation of the turnover and the necessity to conduct analysis on the impact of the concentration over the affected market. *i.e.* the market of manufacture and trade with defence-related products.

By decision^[5] following the instructions of SAC, the BCPC preliminary finds that the transaction indeed meet the notification thresholds under Art. 24, para. 1 of the BCPA. Even further, each of the merging undertakings are considered to have a dominant position on the market of some of the defence-related products being sole manufacturers in the Republic of Bulgaria. As a result, BCPC initiates an in-depth investigation of the transaction.

Only after three-instance-review, BCPC shares concerns that after the merger the aggregate market share of the undertakings concerned may amount to 30-40%. Being two of the five major

producers of defence-related products on the territory of the Republic of Bulgaria, EMKO Ltd. and Dunarit JSC would gain leadership position on the production market after the transaction, having aggregate market share of 30-40%. This amount is relatively close to the 40% market share, presumed by the Methodology[6] to create a dominant position or to strengthen already existing dominance.

Conclusion

The annulled merger control decision comes as a reminder that even at first sight the simple task of turnover calculation can be problematic in practice, and that the national competition authorities and courts are not immune to missteps.

[1] Bulgarian Commission for Protection of Competition Decision No.588/11.08.2016;

[2] Bulgarian Commission for Protection of Competition Order No.216/30.03.2016;

[3] Bulgarian Commission for Protection of Competition Order No.301/11.05.2016;

[4] Methodology for conducting a survey and determining the market position of the undertakings on the relevant market adopted with Bulgarian Commission for Protection of Competition Decision No.393/21.04.2009;

[5] Bulgarian Commission for Protection of Competition Decision No.169/04.02.1019;

[6] Methodology for conducting a survey and determining the market position of the undertakings on the relevant market adopted with Bulgarian Commission for Protection of Competition Decision No.393/21.04.2009

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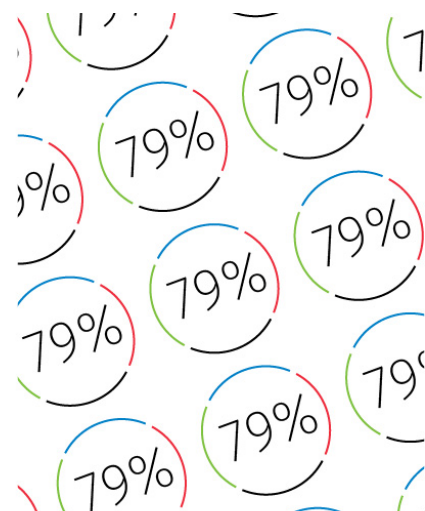
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