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MERGER ASSESSMENT IN THE MIDST OF FINANCIAL CRISIS

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Abstract: *Merger assessment in the midst of a financial crisis is highly challenging. It is important to maintain a rigorous enforcement of the merger rules in order to preserve the competitiveness of European business and facilitate its emergence from the crisis.*
In the first part of this paper we briefly highlighted the concept of economic concentration and the notification procedure for acceptance or rejection. Then, in parallel with the evolution of global mergers and acquisitions activity, we analyzed the number of concentrations that have been notified to the European Commission during the financial crisis. The analyse that follows reveals a reduction in the number of cases but not in their complexity and the specific case of the banking sector - rescue mergers.
Keywords*: merger&acquisitions, merger control, competition policy J.E.L.: F02, K21, L40*

1. INTRODUCTION

The completion of the internal market and of economic and monetary union, the enlargement of the European Union and the lowering of international barriers to trade and investment will continue to result in major corporate reorganisations, particularly in the form of concentrations.

A concentration shall be deemed to arise where a change of control on a lasting basis results from:

(a) the merger of two or more previously independent undertakings or parts of undertakings, or

(b) the acquisition, by one or more persons already controlling at least one undertaking, or by one or more undertakings, whether by purchase of securities or assets, by contract or by any other means, of direct or indirect control of the whole or parts of one or more other undertakings. [COUNCIL REGULATION (EC) No 139/2004].

Such reorganisations are to be welcomed to the extent that they are in line with the requirements of dynamic competition and capable of increasing the competitiveness of European industry, improving the conditions of growth and raising the standard of living in the Community .

However, some mergers may reduce competition in a market, usually by creating or strengthening a dominant player. This is likely to harm consumers through higher prices, reduced choice or less innovation; Community law must therefore include provisions governing those concentrations which may significantly impede effective competition in the common market or in a substantial part of it.

Competition policy has a major role to play in the transition from an economy in crisis that needs public support and aid to the dynamic and sustainable economy the Europe 2020 strategy targets. There can be no sustainable growth within Europe without effective competition in the single market. This is what drives companies to innovate and to expand, for the benefit of consumers, businesses and the European economy as a whole.

2. MERGER ACTIVITY DURING THE CRISES

During the crisis, M&A deals were still being done, but the focus was more on taking advantage of competitive weaknesses and building out the bottom line rather than on strategic growth. Post-crisis, companies are seeking more strategic growth opportunities, particularly in markets such as Asia and Latin America.

In 2007, Mergermarkets estimated the global M&A market to be doing around US$ 3,600 billion worth of mergers in about 15,700 deals. Over the next three years, as the financial markets in the West melted and many industries and geographies witnessed negative growth, the number of mergers as well as the total value went down, to hit $1,800 billion in 9,400 deals in 2009. In short, the total value of deals struck globally halved, while the number of deals came down by 40 percent, indicating that value per deal or the price paid per acquired company has more or less stayed where it was and had not come down dramatically from where it was in 2007, even as the number of deals came down to half. [N. Sharma, 2010]

Against all expectations, the world in 2010 enjoyed a surprisingly benign economic climate. In 2010, corporate merger and acquisition activity made a huge comeback. Most of the M&A activity involved North American companies, but activity has also increased around the world, and in various market sectors / industries.

Companies have stashed away a record amount of cash, which they have hoarded since the height of the financial crisis when cash was considered king. Acquiring companies have been spurred on by record low interest & lending rates, as well as a North American economy which has been considered as "stabilized". Risk in general, has been perceived to be lower than during financial crisis, and there has been an increase in corporate and investor confidence. Even though stock prices were a lot higher in 2010 than in 2008 or 2009, the market value of companies have still remained relatively low due to a weak global economy.

The value of deals in the 12 months through November 2010 rose 9% from the same period ended November 2009, to $786 billion, according to Thomson Reuters. However, the number of deals was flat, and there were few megadeals, owing to uncertainty and perceived levels of risk in the global economy. M&A activity significantly increased during the second half of 2010 especially for large sized (multi-billion dollar) takeovers. Late July and the month of August were notable for heavy merger & acquisition activity. Those months were highlighted by the announcements of : 7/29/2010 – Sanofi-Aventis – Genzyme ($18.5 billion) and 8/14/2010 -BHP Billiton – Potash Corp ($40 billion)

3. Overview of EU Merger Control

A specific legal instrument is necessary to permit effective control of all concentrations in terms of their effect on the structure of competition in the Community and to be the only instrument applicable to such concentrations. Regulation (EEC) No 4064/89 has allowed a Community policy to develop in this field. It was important to maintain a rigorous enforcement of the merger and antitrust rules in order to preserve the competitiveness of European business and facilitate its emergence from the crisis.

The new EU Competition Commissioner Joaquin Almunia noted that mergers and acquisitions play an important role in a competitive and healthy Europe and, for this reason, he said that the Commission should only intervene on the merits of a contemplated transaction where the proposed merger creates competition problems leading to higher prices or less innovation on the market.[J. Almunia, 2010]. Here, we present the legal base: Council Regulation 139/2004:

Procedure for controlling merger operations between enterprises

When to notify?
Either following
· conclusion of the agreement

Phase I deadline commences
· On the date when the complete notification is received by the Commission

Notification
· Mandatory for all concentrations with a Community dimension

Phase I: Initial Examination
· Detailed appraisal via: request for information, interviews, inspections carried out by the competent Authorities of the
Member States and the Commission
· Member States can request referral within 15 working days of notification.

Phase I deadlines
Article 6 decision to be taken
· within 25 working days after receipt of the complete notification
· unless increased to 35 working days if a Member State makes a 9(2) request, or
· unless increased to 35 working days if the undertakings concerned offer commitments

Article 6: decision
· 6(1)a : the concentration does not fall within the scope of the Merger Regulation
· 6(1)b : the concentration does not raise serious doubts as to its compatibility with the common market: approval
· 6(1)c : the concentration raises serious doubts: phase 2 of procedure

interviews, inspections carried out by the competent Authorities of the Member States and the Commission
· Declaration of incompatibility is preceded by the issuing of a statement of objections, with a right for the parties to access the file and to request a formal oral hearing
· Advisory Committee of Member States: meeting and delivery of opinion

Phase II deadlines
Article 8 decision to be taken
· within 90 working days of initiation
of proceedings, or
· within 105 working days if the notifying parties offer commitments later than 55 working days from
initiation of proceedings.
Extension of up to 20 working days upon request by, or with the agreement of, the notifying parties: maximum duration of phase II = 125 working days

Two months from the date of the decision to lodge an appeal

Article 8: final decision
· 8(1): approval in case of compatibility with the common market
· 8(2): approval with conditions and obligations rendering the concentration compatible with the common market
· 8 (3):prohibition in case of incompatibility with the common market
· 8(4): dissolution of the merger in case of premature implementation or implementation in breach of a condition for clearance
· 8(5): interim measures
· 8(6): revocation of a clearance decision in case of incorrect information or breach of obligation.

Possibility: **Review by the European Court of First Instance and ultimately by the European Court of Justice**

A concentration has a Community dimension, if: [Council Regulation (EC) No 139/2004]

- the combined aggregate worldwide turnover (from ordinary activities and after turnover taxes) of all the undertakings concerned (in the case of the acquisition of parts of undertakings, only the turnover relating to the parts which are the subject of the concentration shall be taken into account

In case these thresholds are not met a concentration has nevertheless Community dimension, if:

-the combined aggregate world-wide turnover of all the undertakings concerned is more than EUR 2 500 million, **and**

-in each of at least three Member States, the combined aggregate turnover of all the undertakings concerned is more than EUR 100 million, **and**

-in each of at least three Member States included for the purpose of the second point above, the aggregate turnover of each of at least two of the undertakings concerned is more than EUR 25 million, **and**

-the aggregate Community-wide turnover of each of at least two of the undertakings concerned is more than EUR 100 million, **unless**

-each of the undertakings concerned achieves more than two-thirds of its aggregate Community-wide turnover within one and the same Member State.

EU merger control instruments allow for appropriate application in circumstances of economic crisis, whilst ensuring effectiveness of competition policy. [N. Calviño, 2010]

In the wake of the financial crisis, the Commission was confronted with complex jurisdictional issues under the EC Merger Regulation. Indeed, questions arose as to whether nationalisations of financial institutions needed to be notified to the Commission under the Merger Regulation. This depended on whether or not the nationalised entity would remain an economic unit with an independent power of decision, or whether such nationalised entity could be considered to form part of a single economic entity with other State controlled undertakings. In most cases, the Commission was satisfied that the holding arrangements ensured independence and thus that no concentration was taking place. However, in the German Hypo Real Estate bank case a concentration had to with regard to the seller(s)) is more than EUR 5 000 million **(**special rules apply to banks), **and**

- the aggregate Community-wide turnover of each of at least two of the undertakings concerned is more than EUR 250 million, **unless**

- each of the undertakings concerned achieves more than two-thirds of its aggregate Community-wide turnover within one and the same Member State.

be notified (Case COMP/M.5508 — *SoFFin/Hypo Real Estate*.).

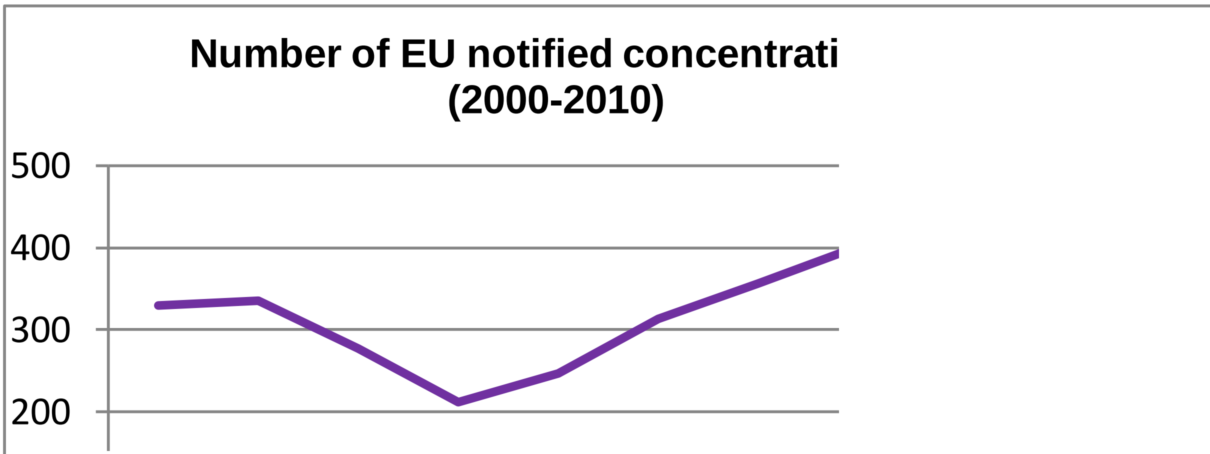
In period of financial crises, in EU merger control, the failing firm defence has not played an important role.

Following the onset of the 2008 financial crisis, governments throughout Europe have intervened in the **merger approval process in a number of cases to enable banking consolidation in the interest of financial stability**. These interventions raise the question of whether competition regulators should be allowed to follow their standard merger approval processes during times of systemic crisis, or whether special procedures are indeed justified.

It is important to recognise the substantial size of the potential costs and risk to the state of measures associated with systemic financial crisis. As an illustration, the governor of the Bank of England, Mervyn King, stated in a speech on 20 October 2009 that: "The sheer scale of support to the banking sector is breathtaking. In the UK, in the form of direct or guaranteed loans and equity investment, it is not far short of a trillion (that is, one thousand billion) pounds, close to two-thirds of the annual output of the entire economy."[P. Bagci, 2010]

The unusual public cost and widespread scale of the impact of bank failures means that exceptions to standard merger regulation may be required during a financial crisis. In circumstances where it is perceived that a merger may substantially reduce the cost to society of dealing with a banking crisis, the system needs to be flexible enough to allow such an intervention by central government. This can be seen as providing the basis for governments to maintain a financial stability public interest test in the merger framework which may, on occasion, allow anti-competitive mergers to take place.

During the recent financial crisis, we can observ a reduction in the number of cases but not in their complexity:



Source: author (upon dates available on European Comision, DG Competition)

In **2009**, the number of mergers notified was below the record levels of previous 78. years. In total, 259 transactions were notified to the Commission and 243 final decisions were adopted. Of these final decisions, 225 transactions were approved without conditions during Phase I, 82 decisions were approved without conditions under the normal procedure and 143 (or 63.6 %) were cleared using the simplified procedure. Thirteen transactions were cleared in Phase I subject to conditions. Furthermore, the Commission initiated five Phase II proceedings, with three decisions adopted subject to conditions. Two cases were withdrawn in Phase II and six cases in Phase I. No prohibition decisions were taken during the year.

As we can see in the chart, in **2010**, the Commission received a total of 274 notifications of proposed transactions meeting the EU thresholds. In 2009, the volume of EU notifications was roughly the same. The busiest year thus far has been 2007 ("pre-crisis"), when the Commission reviewed more than 400 proposed mergers. EU merger control constitutes, in a way, an economic bellwether. [P. Kirch , J. Lucas, 2011]

In 2010 the number of mergers notified was at low level due to the economic crisis. The Commission took three decisions in 2010 following an in-depth analysis in second phase investigation for the Oracle / Sun Microsystems, Monsanto / Syngenta and Unilever / Sara Lee Body mergers (EUROPEAN COMMISSION, COM(2011) 328).

The year 2010 was marked by consistent and stable merger enforcement by the Commission despite the reduction of notified transactions due to the financial and economic crisis.

For just the 21st time in the 20-year history of EU merger control and the first time in more than three years, the European Commission has prohibited a proposed merger outright. On January 26, 2011, the Commission prohibited, on the basis of the EU Merger Regulation, a proposed merger between Greece's two largest airlines: Aegean Airlines and Olympic Air. The Commission considered that the merger would have resulted in a quasi-monopoly on the relevant air transport market since, together, the two carriers control more than 90% of the Greek domestic market. [Commission Decision of January 26, 2011] This is the first prohibition decision since the *Ryanair/Aer Lingus* case in 2007, which also concerned the air transport market.

The economic crisis did not have a substantial impact on the Commission's policy and practice regarding commitments in merger cases. Structural commitments and, notably, divestitures, remained the most appropriate type of remedies in order to prevent, durably, the competition concerns which would have been raised by a merger. In some cases, the Commission, when evaluating a request for the extension of a deadline for the implementation of a remedy, took into account the difficulty of finding buyers in the prevailing economic climate. Similarly, the Commission's merger procedures have proven well suited to their end, also under difficult economic conditions. Notably, the Commission granted six derogations from the standstill obligation in a number of urgent cases having regard to the prevailing economic climate, albeit in full conformity with a well established and strict practice.

4. CONCLUSION

The European Union is undergoing a period of rapid and dramatic changes. Some challenges and issues can be foreseen with some degree of certainty – the exit from the crisis, global competition and sustainable development are among the most prominent. But the EU will no doubt face other challenges which cannot be foreseen yet. Nevertheless, it is clear that competition policy throughout its existence has, against the background of a stable Treaty framework, been able to cope with the considerable evolutions of its environment. Given its resilience and adaptability, EU competition policy will continue to be one of the European Union's assets.

We can expect that will be a substantial increase in mergers and acquisitions in 2011, as companies have plenty of cash to spend on strategic acquisitions, especially in fast-growing emerging markets. Demand for commodities from developed nations, and from emerging markets will contribute to the huge increase. Larger companies from BRIC nations, especially Russia, China, and Brazil, will likely be ones that will acquire smaller companies, rather than be acquired.

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