GERMAN COMPETITION LAW CHANGES: NEW RULES ON MERGER CONTROL, MARKET DOMINANCE, DAMAGES CLAIMS, AND CARTEL FINES

By Andreas Grünwald

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On March 9, 2017, the German Federal Parliament passed the ninth amendment to the Act against Restraints of Competition (ARC) (*Gesetz gegen Wettbewerbsbeschränkungen*). The amendment will come into force in the second quarter of 2017 and will substantially change German competition law.

The reform is driven in part by formal requirements to implement EU legislation into national German law (in particular, provisions of Directive 2014/104/EU, the "Cartel Damages Directive"), and to eliminate some inconsistencies between EU and German law in the area of cartel enforcement. But it also aims to adjust the domestic competition law framework to some of the challenges that come with big data, two-sided markets, and with the digital economy more generally.

For companies and investors doing business in Germany, the new law brings a number of practical changes:

- It introduces a **new transaction value threshold for mergers** to require clearance by the German Federal Cartel Office (FCO) (*Bundeskartellamt*);
- It exempts certain **cooperations among newspaper and magazine publishers** from (German) antitrust scrutiny, aiming to create efficiencies in particular for small and medium size market players.
- It puts an end to certain practices of **avoiding monetary fines** from cartel investigations by restructuring the affected corporate entities;
- It harmonizes the German approach towards **parental liability for cartel fines** with EU law;
- It expands the FCO's tool box to **assess market power** when dealing with "big data" or network effects in digital markets, both in merger cases and in antitrust investigations;
- It introduces a number of changes to the framework for bringing follow-on cartel damages cases in Germany, *e.g.* with respect to the

passing-on defense, disclosure obligations, statute of limitations, plaintiffs' exposure to litigation costs, or settlements.

The reform is the first major competition law change since 2013 and the first relevant change in the area of private cartel enforcement since 2005. However, with digitalization constantly driving market changes, it seems a safe bet that subsequent changes will come within much shorter periods of time. In particular, the new law itself asks that the federal government shall monitor the application of some of the new rules, and report back to Parliament after a three-year period. And prior to the recent reform, although it did eventually not (yet) materialize, there was also a discussion about broadening the FCO's regulatory scope towards a general consumer protection agency.

Details

New Merger Control Rules

From an M&A perspective, the most relevant element of the reform is likely the introduction of an additional merger control threshold.

Traditionally, German merger control follows a pure revenue-based approach to determine whether a proposed transaction is reportable for mandatory FCO clearance. Both parties to the transaction must have combined worldwide revenues of more than €500 million; one party to the transaction (*e.g.*, the buyer) must have German revenues of more than €25 million; and another party to the transaction (*e.g.*, the target) must have German revenues of more than €5 million.

Under the new law, these revenue thresholds will remain in place, and if a transaction meets all three of them, it will continue to be reportable already on these grounds. In addition, the new law introduces a transaction value test to still cover transactions that only meet the higher one of the two domestic thresholds, *i.e.*, where the target has less than € 5 million German revenue. These transactions shall now require FCO clearance if:

- The transaction value exceeds € 400 million (to be determined on the basis of the purchase price as agreed as a cash compensation or in another form, including assumed liabilities); and
- The target has "significant" business in Germany, as demonstrated for example by a strong customer base or substantial R&D activities in Germany.

The purpose of this adjustment is to capture transactions that may not (yet) be sizable by revenue standards, but that may nevertheless have a competitive impact, for example, because they concern some innovative start-up business. According to the new law's official reasoning, which explicitly refers to the Facebook/WhatsApp merger in that respect, it is this type of transactions that triggered the introduction of the additional threshold. However, while Facebook's acquisition of WhatsApp did not trigger the existing turnover thresholds in Germany at the time, the acquisition was notified to the European Commission for a full review under Article 4(5) of the EU Merger Regulation (case COMP/M.7217), as the relevant jurisdictional thresholds in at least three other Member States were satisfied. It was then cleared unconditionally in October 2014.

Facilitating Cooperations in the Publishing Sector

The new law introduces a sector-specific exemption for all non-editorial cooperations (for instance, sale of advertisements) among newspaper and magazine publishers from the cartel ban. Unless they are structured as a formal joint venture (and on that basis, trigger a merger control review), such cooperations shall not be subject to further antitrust scrutiny. According to the official reasoning of the new law, in particular small and medium press companies shall benefit from this relaxation by enhancing their potential for synergies and rationalization.

The publishing industry had successfully lobbied

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for this relief against the background of shrinking advertising and sales revenues in the changing market environment where they are facing increasing competitive pressure from digital media. The new law now therefore potentially allows even hardcore-restrictions (such as price agreements) among publishing houses where they are deemed to be required to preserve the diversity of the press and its ability to compete internationally. During the legislative process, similar exemptions had also been requested in favor of cooperations between public broadcasters and mutual savings banks, but those did not eventually make it into the new law.

With all these sector-specific provisions, however, it must be noted that they can legally only effect the non-application of the cartel ban as provided for in German law, but not a non-application of EU Community-level antitrust law. So wherever a certain sector co-operation has a cross-border dimension to it, it will thus remain subject to full scrutiny under Article 101 of the Treaty on the Functioning of the European Union (TFEU).

Liability and Succession: Closing the "Sausage Gap"

In response to an urgent demand from the FCO, the new law expands the liability for monetary fines in cartel cases. In part, this goes back to a specific case in the German meat industry where the FCO had issued a €130 million fine against a certain corporate entity. As a result of an internal restructuring, the addressee of the fine had then ceased to exist and thereby managed to avoid its liability.

This loophole, commonly referred to as the "sausage gap," will no longer be available. Under the new law, not only the addressee of the fine, but also its legal successor shall be liable for FCO fines and, more generally, the new law establishes a principle of parental liability as it already exists under EU competition law. Accordingly, a parent company can now be held liable for fines that were only imposed on its subsidiary, even where the parent was itself not involved in the competition law infringement or where it did not violate any supervision duties in relation to the subsidiary.

In an M&A context, this will become relevant when it gets to assessing potential liabilities of a target company during due diligence. Specific care should thus be taken where the target in a transaction is (or was) part of a group of companies which had been involved in antitrust infringements. This target might end up being held liable for FCO fines even if it was not itself involved in the infringement or an addressee of the fine. A potential acquirer may want to mitigate such risk by asking the seller for respective indemnities or other safeguards when negotiating the transaction.

Enhanced FCO Tool Box for Assessing Market Power

With a particular focus on dealing with digital businesses, the new law expands the FCO's tool box when it comes to defining markets and assessing market power. These new rules will apply:

- in a *merger control* context when the FCO needs to assess whether a transaction results in a significant impediment to effective competition under the SIEC test; and
- in *investigations of specific business practices* that the FCO might deem to be an abuse of market dominance.

In particular, the new law introduces the following provisions, which to a large extent come as legislative clarifications of practices that the FCO has already developed in more or less established case law over the last few years:

Clarification that it does not require any cash flow between supply and demand side for a "market" to exist. In traditional German case law, a "market" in competition law terms only existed where goods or services were offered for (cash) remuneration. As a consequence, legislative tools for regulating market structures or behaviors did not apply to "free" services. But regulators had already reconsidered this view in recent years, and this is now explicitly reflected in statutory law.

Criteria to determine market power on multi-sided markets. The new law picks up a number of criteria that the FCO's own task force for the digital economy identified as relevant factors to assess an undertaking's role in a given market, namely:

- Direct and indirect network effects;
- Multi-homing (parallel use of services) and users' switching costs;
- Economies of scale in conjunction with network effects;
- Access to competitive data; and
- Innovation-driven competitive pressure.

Again, these concepts are not entirely new, and have at least in part already been applied in recent FCO and court cases.

Overall, these changes will likely not shift the focus of the FCO's merger control and antitrust enforcement, but they may well lower the FCO's threshold for exerting its discretion when launching an investigation into "new" markets or business practices, and help the FCO argue a theory of harm in big data and other "digital" cases. At least indirectly, this may then also have an impact on evaluating the chances to achieve FCO merger control approval for a proposed transaction in these markets.

Implementation of the Cartel Damages Directive (2014/104/EU)

In Europe, participants in anti-competitive conduct increasingly see themselves confronted with so-called follow-on litigation, where customers claim compensation for the overcharge that they paid for cartelized products or services. Where a cartel has been sanctioned by the EU Commission or a Member State competition authority, such claims benefit from the binding effect of the infringement decision. In court, the plaintiff then only has to establish the amount of damages occurred, but not the existence of the cartel as such.

Until now, the legal framework to bring such cartel damages claims varies among EU Member States, with Germany, the Netherlands, and the UK being the preferred venues for plaintiffs. To harmonize these standards, and to encourage damages claims as "private enforcement" of antitrust laws, the EU Commission therefore adopted the Cartel Damages Directive in late 2014. Germany is already late in implementing the Directive into national law (the two-year implementation period lapsed on December 27, 2016), which will now happen as a key element of the new German competition law.

Key changes to the legal framework for bringing cartel damages claims under German law include:

- ***Rebuttable presumption of harm***: It shall be legally assumed that cartel infringements generally lead to damages but the infringer shall have the right to rebut this assumption. The assumption shall apply to the existence of the harm as such and to the causality link with the infringement, but not to the actual amount of damages caused.
- ***Passing-on defense***: The new law specifies the principle of the passing-on defense, and also facilitates it compared to the existing standards as developed in German case law. Accordingly, the defendant in an action for damages can invoke that the claimant passed on the whole or parts of the overcharge to its own customers, but the defendant shall bear the burden of proof to establish the underlying facts for this defense.
- ***Claims from indirect purchasers***: By specify-

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ing the passing-on rules, the new law also facilitates claims from indirect purchasers. It introduces a statutory presumption for the benefit of the indirect purchaser that the direct purchaser passed on the overcharge.

- ***Disclosure requirements***: The new law introduces certain tools for both the claimant and the defendant in a cartel damages case to require the respective other party to disclose some of its internal documents and calculations. This disclosure claim can be enforced together with, or separately from, the damages claim, including by way of preliminary injunction.

- ***Statute of limitations***: Under legacy German law, cartel damages claims became time-barred within three years from the end of the calendar year in which the damages claim arose and if the claimant knew (of should have known) about the relevant underlying facts. The new law extends this limitation period from three to five years.

- ***Joint and several liability***: The new law introduces some exemptions from the general principle that the participants in a cartel shall be jointly and severally liable for the full amount of damages caused by the cartel. Going forward, the joint and several liability of small and medium enterprises, as well as recipients of full immunity during the infringement proceedings, shall generally be limited to their own direct or indirect sales.

- ***Settlement effects***: Under existing German law, there is a risk for each cartelist that a settlement with one claimant will still not prevent the other cartelists from bringing contribution claims against the settling defendant. The new law makes settlements binding upon the other cartelists to the extent that the share of damages settled is concerned. This will make individual settlements for cartelists more attractive.

- ***Plaintiffs' exposure to litigation costs***: The "loser pays" principle applies in German civil proceedings, *i.e.*, the plaintiff faces the risk of having to cover the statutory attorneys' fees for all defendants. In cartels with many members, the plaintiff therefore faced a considerable cost risk, which is now being reduced by the new law. The losing plaintiff will only have to pay the statutory attorneys' fees of the actual defendant(s) and one intervenor.

These changes will obviously not have a primary impact on M&A activity. But again, like with the enhanced rules on cartel fines, liability risks from private antitrust enforcement may still become a diligence issue when assessing a proposed transaction.

Outlook

After almost two years of intense discussions in the antitrust community, and at least in part guided by a dedicated EU law framework, the new German competition law generally comes with few surprises; but it still contains a number of paradigm shifts that will have material practical implications going forward.

With regard to merger control, the supplemental transaction value test is less clear than the existing revenue-based filing thresholds. Even where the lower domestic revenue threshold is not met, the parties to a transaction will still have to apply further efforts to determine whether a filing would be required. At least until some further FCO guidance is available on the new criteria, we will likely see more German filings even in smaller cases, just because the merging parties want to mitigate any potential risk of violating filing (and gun-jumping) requirements. Also, it remains to be noted that German merger control does not only apply to transactions that result in a change of control over the target company. As long as the revenue thresholds (or, going forward, the transaction value test) are met, even the acquisition of a minority shareholding in the target company would be reportable to the FCO, provided that the buyer acquires at least 25% of the capital or voting rights or otherwise gains "relevant competitive influence" over the target business.

Beyond merger control, where the new law adopts a number of principles from recent case law with respect to market definitions and assessing dominance, these additions will not have an immediate impact on the business community. Nevertheless, the changes may still pave the way for the FCO to continue, and maybe even intensify, its sometimes-tough approach toward the digital economy. Here, the new framework may help the FCO to come up with a more robust theory of harm and to ultimately defend it in court.

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