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Brexit: merger review implications and recommendations

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The United Kingdom's vote to leave the European Union – known as Brexit – triggered a political and economic earthquake whose political and economic consequences continue to make daily headlines, almost five months later.

Although the long-term consequences of Brexit will not become clear for many years, one antitrust-related consequence will be of particular interest to multinational businesses: elimination of the "one-stop-shop" of the European Union's Regulation 139/2004 on the control of concentrations among undertakings (the EUMR).[1]

Under the current system, a Brussels filing precludes the need to file in the United Kingdom. In future, many transactions that are notified under the EUMR will also be notified to the UK Competition and Markets Authority (CMA). This duplication of notification requirements will increase the already significant burdens for companies engaged in mergers or acquisitions, who will have to make parallel filings in Brussels and London. The burden of duplicate merger notifications will be particularly significant in major strategic transactions in the agricultural sector, such as Bayer/Monsanto, ChemChina/Syngenta, and Dow/DuPont, which may involve multiple markets and complex vertical and joint venture relationships.

In this article, we explore the merger control implications of Brexit in more detail and offer some preliminary suggestions of ways to mitigate the burden on competition authorities and business.

Background

The basic mechanism for an EU Member State to leave the European Union is set out in Article 50 of the Treaty on the European Union (TEU), but the language of this article is very general.[2] The Article 50 process is triggered by a notice from the leaving Member State to the European Council. Once the notice is given, the departing State has two years to negotiate an exit agreement, failing which its exit becomes effective automatically. The complexity of the issues involved makes it highly unlikely that an agreement can be reached in less than two years.

Prime Minister Theresa May has said that the UK will give this notice by March 2017, so the effective date for the United Kingdom's exit from the European Union will likely be around March 2019. In addition to the exit agreement, the UK and the EU will need to negotiate a more comprehensive agreement to govern their future relationship, such as a customs union or free trade agreement. While the exit agreement can be approved by a qualified majority vote in the European Council, the future comprehensive agreement will likely need to be approved unanimously and ratified by each remaining EU Member State, a process that could drag on for many years.

The broader consequences of Brexit and the future relationship between the EU and the UK are beyond the scope of this article. For present purposes, however, it seems reasonable to assume that as from March 2019 EU merger notifications will no longer cover the UK. As a result, parties to M&A transactions triggering the EUMR thresholds will also have to consider the application of the UK merger regime, which is structured very differently.

The key difference between the EU and UK systems lies in which mergers are caught in the first place. The UK system captures "relevant merger situations" where the target has turnover above £70 million, or the combined market share of the parties on any plausible market definition is twenty-five percent or more. In those situations, parties can decide whether or not to notify the CMA. In practice, parties who meet the test are well-advised to inform the CMA, even if by an informal letter explaining why the parties do not intend to notify formally. The CMA can, wherever a relevant merger situation

1 Council Regulation (EC) No 139/2004 of January 20, 2004 on the Control of Concentrations between Undertakings.

2 Article 50 of the TEU, available at http://www.lisbon-treaty.org/wcm/the-lisbon-treaty/treaty-on-European-union-and-comments/title-6-final-provisions/137-article-50.html

occurs, call in a merger for review. By contrast, if a deal meets the EU notification thresholds – which are currently entirely turnover-based[3] – an EU notification is mandatory. Moreover, the parties cannot close a deal until EU clearance has been obtained: in the United Kingdom, it is legal to close a deal qualifying as a relevant merger situation, although the CMA will likely require the parties in a case that the CMA is investigating to hold their businesses separate until a decision has been reached.

The differences between the thresholds affect the types of mergers reviewed by each authority. For example, under the EUMR so-called "full function joint ventures" may be notifiable based on the parent companies' turnover even where the joint venture itself is small and has little or no presence in the EU and/or where there is no overlap in the parties' activities. Cases of this nature are not caught under the UK rules.

These structural differences are reflected in the outcomes of cases reviewed under the UK and EU systems. The CMA conducts in-depth investigations in a much higher percentage of transactions, reflecting the fact that the CMA's case load includes a higher proportion of difficult cases, as routine cases presenting no serious issues cases are often not notified. Similarly, a far larger proportion of CMA decisions require remedies or commitments to resolve competition concerns than is the case in Brussels. Because the CMA's cases are more difficult, on the whole, the CMA has a number of different processes from the Commission:

- The CMA can fast-track cases straight to the in-depth Phase 2 review, where it is clear that the deal could not be cleared in Phase 1. [4]
- The CMA has no "short form" notification procedure. At the EU level, parties to deals that on their face raise no concerns can use the less onerous "Short Form CO," an abbreviated version of the full Form CO used for notifying transactions under the EUMR. Indeed, the Commission even exempts notifying parties from complying with all aspects of the Short Form CO in the most straightforward cases.
- The CMA's Phase 1 review lasts forty working days, compared to the Commission's twenty-five. The CMA's longer review period may be off-set, however, by the Commission's practice of engaging in (sometimes lengthy) pre-notification discussions, which take place before the Commission accepts the notification as complete. In essence, this allows the Commission to extend the review process outside the statutory timetable.

Finally, the United Kingdom retains a narrow role for public interest factors like national security, plurality of the media and preserving stability of financial markets, but Theresa May has suggested that UK merger review should take more account of "industrial strategy." By contrast, the EU regime carves out public interest factors as an issue for Member States and so there is (at least in theory) no scope for policy issues to intrude on EUMR reviews.

Brexit Consequences for Merger Control

The elimination of the UK from the EUMR one-stop-shop can be expected to lead to a significant increase in the number of UK filings post-Brexit, though not all transactions notified in the EU will also be notified in the UK.

While many if not most transactions that meet the EU thresholds are also likely to meet the UK thresholds, although transactions clearly raising no competition issues, like many private equity transactions, will probably not need to be notified in the United Kingdom. Moreover, some transactions having a "Union dimension" under the EUMR may not meet the UK test. For instance, joint ventures that meet the EU turnover thresholds by virtue of the parents' turnover are not necessarily captured under the UK rules. In addition, many deals that meet the EU thresholds will not trigger the UK thresholds, because the target does not have more than £70m in UK turnover and the transaction does not involve the creation or increase of a twenty-five percent share of supply in the United Kingdom.

Conversely, Brexit may lead to a slight reduction in the number of EU filings. Many companies derive a significant portion of their EU turnover in the United Kingdom, and some transactions that would currently be notifiable under the EUMR will likely not meet the turnover thresholds for mandatory filing when the United Kingdom is excluded. Perhaps more significantly the number of EU filings made pursuant to a voluntary referral request may be reduced. Under the EUMR, parties acquiring control in transactions that would otherwise be notifiable in three or more Member States can request that the transaction be referred to the Commission for review. The United Kingdom's jurisdictional thresholds are broad, and it is not uncommon for the United Kingdom to count as one of the jurisdictions that can be used to trigger a referral request. The parties to

3 EUMR, Article 1(2) & (3). The European Commission is currently consulting on the possible introduction of a deal-size threshold, which may be in effect by 2019.

4 This fast track process was first used in Thomas Cook/Co-op/Midlands Co-operative Society Thomas Cook/Co-op/Midlands Co-operative Society Merger Inquiry (CC) August 16, 2011.

transactions that would be subject to review in only three EU Member States, one of which is the United Kingdom, would no longer be able to take advantage of the referral process.

Overall, while it is not possible to predict with any accuracy the likely effect on the number of EU merger filings based on data published by the Commission, it seems likely that Brexit will result in a small but noticeable drop in the number of filings to Brussels.

Divergent outcomes and resulting burden on businesses

One theoretical possibility that will raise material concerns for business is the increased possibility of concurrent reviews in London and Brussels leading to divergent outcomes (i.e., one authority clearing a merger and the other blocking it) and/or of differing, inconsistent remedies. A recent example of such divergent outcomes involved Eurotunnel's acquisition of the bankrupt SeaFrance ferry operation, which was approved by the French authorities but blocked by the United Kingdom.[5]

Currently, Section 60 of the UK Competition Act 1998 contains a "convergence clause" to ensure the compatibility of UK competition law with EU competition law. Post-Brexit, there will be no legal need for such a clause, and it might be removed from UK law. Removal of the convergence clause would increase the likelihood of the CMA's approach diverging from the Commission's in specific cases, although both authorities will presumably strive to avoid such divergent outcomes.

5 CMA Update of January 20, 2016 in Eurotunnel / SeaFrance Merger Inquiry, https://www.gov.uk/cma-cases/eurotunnel-seafrance-merger-inquiry

Elimination from the European Competition Network

Another significant consequence of Brexit would be the removal of the CMA from the European Competition Network (ECN), which includes the Commission and EU Member State competition authorities. Two notable advantages of the ECN are (i) close co-operation and consistency among national competition authorities such as the CMA and (ii) a flexible and informal case allocation system. Leaving the ECN will mean this close cooperation and consistency will be lost, with, importantly, both the CMA and the other national authorities losing out.

In summary, Brexit may somewhat reduce the number of EU filings, but Brexit will likely lead to a significant increase in the number of UK notifications. The duplication of work and the risk of divergent timetables and (potentially) outcomes will impose significant additional costs on businesses and (in some cases) increase legal uncertainty for business.

Mitigating the "Brexit Tax" in Merger Review

Although Brexit seems likely to increase the burdens of the merger review process and in some cases to increase legal uncertainty, there are some concrete steps that could be taken to mitigate these negative consequences. Some of these steps are discussed below.

One key step that the Commission and the CMA can and, in our view, should take is to create an ad hoc framework for cooperation in merger cases. This framework should provide for close cooperation between the Commission and the CMA in cases notified to both jurisdictions, beginning well before the Commission's existing procedures for consulting EU Member State authorities on proposed merger decisions. To reduce the duplication of effort for themselves and for businesses, for example, the Commission and the CMA could consult on the information to be included in a complete notification.

The CMA could also agree that it would accept EU notifications (with some supplemental UK-specific information) for UK purposes. The Swiss competition authority already follows such an approach in respect of transactions that have also been filed in Brussels.

Similarly, the Commission and the CMA could cooperate in the collection of evidence. For instance, they could prepare common questionnaires, cooperate in interviews with customers and competitors, and conduct site visits and state-of-play meetings jointly. The U.S. and Canadian authorities embrace such practices to facilitate their parallel merger reviews.

In each of these cases, the parties' rights of defense would need to be protected, but merging parties would benefit from close cooperation in many if not most cases.

In the relatively small percentage of cases raising substantive issues, cooperation may be more challenging, but offer even greater potential efficiencies. If the recipients of an EU statement of objections wished to exercise their right to an oral hearing, for example, the hearing could be coordinated with the CMA – or, perhaps more realistically, the CMA could consult closely with the Commission and adjust its review timelines to allow the EU and UK processes to move forward in parallel and align key decision points. As noted, the current UK process is forty working days in Phase 1 in comparison to twenty-five working days in Brussels, which will mean the Commission may have had to conclude on whether to open a

Phase 2 investigation before the CMA has reached the same point. It would be in the interests of all parties if such decision making could be better aligned.

Where the parties wish or are required to submit remedies to obtain merger clearance, the Commission and the CMA could agree to accept remedy proposals in the same format, if and to the extent the issues are the same. The Commission and the CMA could also agree to cooperate in the market testing of proposed remedies. Similarly, in remedy implementation the Commission and the CMA could agree to accept the same forms and otherwise avoid duplication. For example, in many cases only one monitoring or divestiture trustee should be required for both the EU and UK processes.

In many cases, we anticipate that it would make sense for the CMA to rely on the Commission's existing precedents and procedures. A useful model might be the existing arrangements under which the Canadian Competition Bureau sometimes relies on remedies negotiated by the U.S. agencies based on a side letter, without the need for a complete separate remedy process in Canada.

Conclusion

In summary, Brexit will likely lead to duplicate EU and UK notifications in many transactions that meet the EUMR thresholds. The additional notification requirements will very likely lead to increased costs and complexity for business and may put a strain on the CMA's resources. With creativity and good will, however, the Commission and the CMA could do much to mitigate these burdens. In many cases, the Commission and the CMA could potentially make significant improvements through bilateral agreements without the need for new legislation.

It remains to be seen how far the CMA will be prepared to accept the Commission as the "lead authority" on European competition matters. The CMA may be less willing to allow another agency to take a leading role than the Swiss and Canadian authorities have been. If that turns out to be the case, a looser structure in which the Commission and the CMA could agree on a case-by-case basis which authority is best placed to take the leading role may be preferable.

Although the structure and contents of the broader Brexit negotiations are likely to be unclear for some time, we encourage the Commission and the CMA to consider potential steps and to set up working groups to discuss these initiatives in parallel with or potentially even before the commencement of the broader negotiations.

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