COMMISSION NOTICE

on the concept of concentration under Council Regulation (EEC) No 4064/89 on the control of concentrations between undertakings

(98/C 66/02)

(Text with EEA relevance)

I. INTRODUCTION

1. The purpose of this Notice is to provide guidance as to how the Commission interprets the term 'concentration' used in Article 3 of Council Regulation (EEC) No 4064/89 [1] as last amended by Regulation (EC) No 1310/97 [2] (hereinafter referred to as 'the Merger Regulation'). This formal guidance on the interpretation of Article 3 should enable firms to establish more quickly, in advance of any contact with the Commission, whether and to what extent their operations may be covered by Community merger control.

This Notice replaces the Notice on the notion of a concentration [3].

This Notice deals with paragraphs (1), (3), (4) and (5) of Article 3. The interpretation of Article 3 in relation to joint ventures, dealt with in particular under Article 3(2), is set out in the Commission's Notice on the concept of full-function joint ventures.

2. The guidance set out in this Notice reflects the Commission's experience in applying the Merger Regulation since it entered into force on 21 December 1990. The principles contained here will be applied and further developed by the Commission in individual cases.

3. According to recital 23 to Regulation (EEC) No 4064/89, the concept of concentration is defined as covering only operations which bring about a lasting change in the structure of the undertakings concerned. Article 3(1) provides that such a structural change is brought about either by a

[1] OJ L 395, 30.12.1989, p. 1, corrected version OJ L 257, 21.9.1990, p. 13.
[2] OJ L 180, 9.7.1997, p. 1.
[3] OJ C 385, 31.12.1994, p. 5.

merger between two previously independent undertakings or by the acquisition of control over the whole or part of another undertaking.

4. The determination of the existence of a concentration under the Merger Regulation is based upon qualitative rather than quantitative criteria, focusing on the concept of control. These criteria include considerations of both law and fact. It follows, therefore, that a concentration may occur on a legal or a *de facto* basis.

5. Article 3(1) of the Merger Regulation defines two categories of concentration:

— those arising from a merger between previously independent undertakings (point (a));

— those arising from an acquisition of control (point (b)).

These are treated respectively in Sections II and III below.

II. MERGERS BETWEEN PREVIOUSLY INDEPENDENT UNDERTAKINGS

6. A merger within the meaning of Article 3(1)(a) of the Merger Regulation occurs when two or more independent undertakings amalgamate into a new undertaking and cease to exist as separate legal entities. A merger may also occur when an undertaking is absorbed by another, the latter retaining its legal identity while the former ceases to exist as a legal entity.

7. A merger within the meaning of Article 3(1)(a) may also occur where, in the absence of a legal merger, the combining of the activities of previously independent undertakings results in the creation of a single economic unit [4]. This may arise in particular where two or more undertakings, while retaining their individual legal personalities, establish contractually a common economic management [5]. If this leads to a *de facto* amalgamation of the undertakings concerned into a genuine common economic unit, the operation is considered to be a merger. A prerequisite for the determination of a common economic unit is the existence of a permanent, single economic management. Other relevant factors may include internal profit and loss compensation as between the various undertakings within the group, and their joint liability externally. The *de facto* amalgamation may be reinforced by cross-shareholdings between the undertakings forming the economic unit.

III. ACQUISITION OF CONTROL

8. Article 3(1)(b) provides that a concentration occurs in the case of an acquisition of control. Such control may be acquired by one undertaking acting alone or by two or more undertakings acting jointly.

Control may also be acquired by a person in circumstances where that person already controls (whether solely or jointly) at least one other undertaking or, alternatively, by a combination of persons (which controls another undertaking) and/or undertakings. The term 'person' in this context extends to public bodies [6] and private entities, as well as individuals.

As defined, a concentration within the meaning of the Merger Regulation is limited to changes in control. Internal restructuring within a group of companies, therefore, cannot constitute a concentration.

An exceptional situation exists where both the acquiring and acquired undertakings are public companies owned by the same State (or by the same public body). In this case, whether the operation is to be regarded as an internal restructuring depends in turn on the question whether both undertakings were formerly part of the same economic unit within the meaning of recital 12 to Regulation (EEC) No 4064/89. Where the undertakings were formerly part of different economic units having an independent power of

(4) In determining the previous independence of undertakings, the issue of control may be relevant. Control is considered generally in paragraphs 12 *et seq*. below. For this specific issue, minority shareholders are deemed to have control if they have previously obtained a majority of votes on major decisions at shareholders meetings. The reference period in this context is normally three years.

(5) This could apply for example, in the case of a 'Gleichordnungskonzern' in German law, certain 'Groupements d'Intérêt Economique' in French law, and certain partnerships.

(6) Including the State itself, e. g. Case IV/M.157 — Air France/Sabena, of 5 October 1992 in relation to the Belgian State, or other public bodies such as the Treuhand in Case IV/M.308 — Kali und Salz/MDK/Treuhand, of 14 December 1993.

decision, the operation will be deemed to constitute a concentration and not an internal restructuring ([7]). Such independent power of decision does not normally exist, however, where the undertakings are within the same holding company ([8]).

9. Whether an operation gives rise to an acquisition of control depends on a number of legal and/or factual elements. The acquisition of property rights and shareholders' agreements are important, but are not the only elements involved: purely economic relationships may also play a decisive role. Therefore, in exceptional circumstances, a situation of economic dependence may lead to control on a *de facto* basis where, for example, very important long-term supply agreements or credits provided by suppliers or customers, coupled with structural links, confer decisive influence ([9]).

There may also be acquisition of control even if it is not the declared intention of the parties ([10]). Moreover, the Merger Regulation clearly defines control as having 'the possibility of exercising decisive influence' rather than the actual exercise of such influence.

10. Control is nevertheless normally acquired by persons or undertakings which are the holders of the rights or are entitled to rights conferring control (Article 3(4)(a)). There may be exceptional situations where the formal holder of a controlling interest differs from the person or undertaking having in fact the real power to exercise the rights resulting from this interest. This may be the case, for example, where an undertaking uses another person or undertaking for the acquisition of a controlling interest and exercises the rights through this person or undertaking, even though the latter is formally the holder of the rights. In such a situation, control is acquired by the undertaking which in reality is behind the operation and in fact enjoys the power to control the target undertaking (Article 3(4)(b)). The evidence needed to establish this type of indirect control may include factors such as the source of financing or family links.

11. The object of control can be one or more undertakings which constitute legal entities, or the assets of such entities, or only some of these assets ([11]). The assets in question, which could be brands or licences, must constitute a business to which a market turnover can be clearly attributed.

12. The acquisition of control may be in the form of sole or joint control. In both cases, control is defined as the possibility of exercising decisive influence on an undertaking on the basis of rights, contracts or any other means (Article 3(3)).

1. Sole control

13. Sole control is normally acquired on a legal basis where an undertaking acquires a majority of the voting rights of a company. It is not in itself significant that the acquired shareholding is 50 % of the share capital plus one share ([12]) or that it is 100 % of the share capital ([13]). In the absence of other elements, an acquisition which does not include a majority of the voting rights does not normally confer control even if it involves the acquisition of a majority of the share capital.

14. Sole control may also be acquired in the case of a 'qualified minority'. This can be established on a legal and/or *de facto* basis.

On a legal basis it can occur where specific rights are attached to the minority shareholding. These may be preferential shares leading to a majority of the voting rights or other rights enabling the minority shareholder to determine the strategic commercial behaviour of the target company, such as the power to appoint more than half of the members of the supervisory board or the administrative board.

([7]) Case IV/M.097 — Péchiney/Usinor, of 24 June 1991; Case IV/M.216 — CEA Industrie/France Telecom/SGS-Thomson, of 22 February 1993.
([8]) See paragraph 55 of the Notice on the concept of undertakings concerned.
([9]) For example, in the Usinor/Bamesa decision adopted by the Commission under the ECSC Treaty. See also Case IV/M.258 — CCIE/GTE, of 25 September 1992, and Case IV/M.697 — Lockheed Martin Corporation/Loral Corporation, of 27 March 1996.
([10]) Case IV/M.157 — Air France/Sabena, of 5 October 1992.
([11]) Case IV/M.286 — Zürich/MMI, of 2 April 1993.
([12]) Case IV/M.296 — Crédit Lyonnais/BFG Bank, of 11 January 1993.
([13]) Case IV/M.299 — Sara Lee/BP Food Division, of 8 February 1993.

A minority shareholder may also be deemed to have sole control on a *de facto* basis. This is the case, for example, where the shareholder is highly likely to achieve a majority at the shareholders' meeting, given that the remaining shares are widely dispersed ([14]). In such a situation it is unlikely that all the smaller shareholders will be present or represented at the shareholders' meeting. The determination of whether or not sole control exists in a particular case is based on the evidence resulting from the presence of shareholders in previous years. Where, on the basis of the number of shareholders attending the shareholders' meeting, a minority shareholder has a stable majority of the votes at this meeting, then the large minority shareholder is taken to have sole control ([15]).

Sole control can also be exercised by a minority shareholder who has the right to manage the activities of the company and to determine its business policy.

15. An option to purchase or convert shares cannot in itself confer sole control unless the option will be exercised in the near future according to legally binding agreements ([16]). However, the likely exercise of such an option can be taken into account as an additional element which, together with other elements, may lead to the conclusion that there is sole control.

16. A change from joint to sole control of an undertaking is deemed to be a concentration within the meaning of the Merger Regulation because decisive influence exercised alone is substantially different from decisive influence exercised jointly ([17]). For the same reason, an operation involving the acquisition of joint control of one part of an undertaking and sole control of another part is in principle regarded as two separate concentrations under the Merger Regulation ([18]).

17. The concept of control under the Merger Regulation may be different from that applied in specific areas of legislation concerning, for example, prudential rules, taxation, air transport or the media. In addition, national legislation within a Member State may provide specific rules on the structure of bodies representing the organisation of decision-making within an undertaking, in particular, in relation to the rights of representatives of employees. While such legislation may confer some power of control upon persons other than the shareholders, the concept of control under the Merger Regulation is related only to the means of influence normally enjoyed by the owners of an undertaking. Finally, the prerogatives exercised by a State acting as a public authority rather than as a shareholder, in so far as they are limited to the protection of the public interest, do not constitute control within the meaning of the Merger Regulation to the extent that they have neither the aim nor the effect of enabling the State to exercise a decisive influence over the activity of the undertaking ([19]).

2. **Joint control**

18. As in the case of sole control, the acquisition of joint control (which includes changes from sole control to joint control) can also be established on a legal or *de facto* basis. There is joint control if the shareholders (the parent companies) must reach agreement on major decisions concerning the controlled undertaking (the joint venture).

19. Joint control exists where two or more undertakings or persons have the possibility of exercising decisive influence over another undertaking. Decisive influence in this sense normally means the power to block actions which determine the strategic commercial behaviour of an undertaking. Unlike sole control, which confers the power upon a specific shareholder to determine the strategic decisions in an undertaking, joint control is characterized by the possibility of a deadlock situation resulting from the power of two or more parent companies to reject proposed strategic decisions. It follows, therefore, that these shareholders must reach a common understanding in determining the commercial policy of the joint venture.

([14]) Case IV/M.025 — Arjomari/Wiggins Teape, of 10 February 1990.
([15]) Case IV/M.343 — Société Générale de Belgique/Générale de Banque, of 3 August 1993.
([16]) Judgment in Case T 2/93, *Air France* v. *Commission* [1994] ECR II-323.
([17]) This issue is dealt with in paragraphs 30, 31 and 32 of the Notice on the concept of undertakings concerned.
([18]) Case IV/M.409 — ABB/Renault Automation, of 9 March 1994.
([19]) Case IV/M.493 — Tractebel/Distrigaz II, of 1 September 1994.

2.1. *Equality in voting rights or appointment to decision-making bodies*

20. The clearest form of joint control exists where there are only two parent companies which share equally the voting rights in the joint venture. In this case, it is not necessary for a formal agreement to exist between them. However, where there is a formal agreement, it must be consistent with the principle of equality between the parent companies, by laying down, for example, that each is entitled to the same number of representatives in the management bodies and that none of the members has a casting vote ([20]). Equality may also be achieved where both parent companies have the right to appoint an equal number of members to the decision-making bodies of the joint venture.

2.2. *Veto rights*

21. Joint control may exist even where there is no equality between the two parent companies in votes or in representation in decision-making bodies or where there are more than two parent companies. This is the case where minority shareholders have additional rights which allow them to veto decisions which are essential for the strategic commercial behaviour of the joint venture ([21]). These veto rights may be set out in the statute of the joint venture or conferred by agreement between its parent companies. The veto rights themselves may operate by means of a specific quorum required for decisions taken at the shareholders' meeting or by the board of directors to the extent that the parent companies are represented on this board. It is also possible that strategic decisions are subject to approval by a body, e.g. supervisory board, where the minority shareholders are represented and form part of the quorum needed for such decisions.

22. These veto rights must be related to strategic decisions on the business policy of the joint venture. They must go beyond the veto rights normally accorded to minority shareholders in order to protect their financial interests as investors in the joint venture. This normal protection of the rights of minority shareholders is related to decisions on the essence of the joint venture, such as changes in the statute, an increase or decrease in the capital or liquidation. A veto right, for example, which prevents the sale or winding-up of the joint venture does not confer joint control on the minority shareholder concerned ([22]).

23. In contrast, veto rights which confer joint control typically include decisions and issues such as the budget, the business plan, major investments or the appointment of senior management. The acquisition of joint control, however, does not require that the acquirer has the power to exercise decisive influence on the day-to-day running of an undertaking. The crucial element is that the veto rights are sufficient to enable the parent companies to exercise such influence in relation to the strategic business behaviour of the joint venture. Moreover, it is not necessary to establish that an acquirer of joint control of the joint venture will actually make use of its decisive influence. The possibility of exercising such influence and, hence, the mere existence of the veto rights, is sufficient.

24. In order to acquire joint control, it is not necessary for a minority shareholder to have all the veto rights mentioned above. It may be sufficient that only some, or even one such right, exists. Whether or not this is the case depends upon the precise content of the veto right itself and also the importance of this right in the context of the specific business of the joint venture.

Appointment of management and determination of budget

25. Normally the most important veto rights are those concerning decisions on the appointment of the management and the budget. The power to co-determine the structure of the management confers upon the holder the power to exercise decisive influence on the commercial policy of an undertaking. The same is true with respect to decisions on the budget since the budget determines the precise framework of the activities of the joint venture and, in particular, the investments it may make.

Business plan

26. The business plan normally provides details of the aims of a company together with the measures to

([20]) Case IV/M.272 — Matra/CAP Gemini Sogeti, of 17 March 1993.

([21]) Case T 2/93 — Air France v Commission (ibid). Case IV/M.010 — Conagra/Idea, of 3 May 1991.

([22]) Case IV/M.062 — Eridania/ISI, of 30 July 1991.

be taken in order to achieve those aims. A veto right over this type of business plan may be sufficient to confer joint control even in the absence of any other veto right. In contrast, where the business plan contains merely general declarations concerning the business aims of the joint venture, the existence of a veto right will be only one element in the general assessment of joint control but will not, on its own, be sufficient to confer joint control.

Investments

27. In the case of a veto right on investments, the importance of this right depends, first, on the level of investments which are subject to the approval of the parent companies and, secondly, on the extent to which investments constitute an essential feature of the market in which the joint venture is active. In relation to the first criterion, where the level of investments necessitating approval of the parent companies is extremely high, this veto right may be closer to the normal protection of the interests of a minority shareholder than to a right conferring a power of co-determination over the commercial policy of the joint venture. With regard to the second, the investment policy of an undertaking is normally an important element in assessing whether or not there is joint control. However, there may be some markets where investment does not play a significant role in the market behaviour of an undertaking.

Market-specific rights

28. Apart from the typical veto rights mentioned above, there exist a number of other veto rights related to specific decisions which are important in the context of the particular market of the joint venture. One example is the decision on the technology to be used by the joint venture where technology is a key feature of the joint venture's activities. Another example relates to markets characterised by product differentiation and a significant degree of innovation. In such markets, a veto right over decisions relating to new product lines to be developed by the joint venture may also be an important element in establishing the existence of joint control.

Overall context

29. In assessing the relative importance of veto rights, where there are a number of them, these rights should not be evaluated in isolation. On the contrary, the determination of whether or not joint control exists is based upon an assessment of these rights as a whole. However, a veto right which does not relate either to commercial policy and strategy or to the budget or business plan cannot be regarded as giving joint control to its owner ([23]).

2.3. *Joint exercise of voting rights*

30. Even in the absence of specific veto rights, two or more undertakings acquiring minority shareholdings in another undertaking may obtain joint control. This may be the case where the minority shareholdings together provide the means for controlling the target undertaking. This means that the minority shareholders, together, will have a majority of the voting rights; and they will act together in exercising these voting rights. This can result from a legally binding agreement to this effect, or it may be established on a *de facto* basis.

31. The legal means to ensure the joint exercise of voting rights can be in the form of a holding company to which the minority shareholders transfer their rights, or an agreement by which they undertake to act in the same way (pooling agreement).

32. Very exceptionally, collective action can occur on a *de facto* basis where strong common interests exist between the minority shareholders to the effect that they would not act against each other in exercising their rights in relation to the joint venture.

33. In the case of acquisitions of minority shareholdings, the prior existence of links between the minority shareholders or the acquisition of the shareholdings by means of concerted action will be factors indicating such a common interest.

34. In the case where a new joint venture is established, as opposed to the acquisition of minority shareholdings in a pre-existing company, there is a higher probability that the parent

([23]) Case IV/M.295 — SITA-RPC/SCORI, of 19 March 1993.

companies are carrying out a deliberate common policy. This is true, in particular, where each parent company provides a contribution to the joint venture which is vital for its operation (e. g. specific technologies, local know-how or supply agreements). In these circumstances, the parent companies may be able to operate the joint venture with full cooperation only with each other's agreement on the most important strategic decisions even if there is no express provision for any veto rights. The greater the number of parent companies involved in such a joint venture, however, the more remote is the likelihood of this situation occurring.

35. In the absence of strong common interests such as those outlined above, the possibility of changing coalitions between minority shareholders will normally exclude the assumption of joint control. Where there is no stable majority in the decision-making procedure and the majority can on each occasion be any of the various combinations possible amongst the minority shareholders, it cannot be assumed that the minority shareholders will jointly control the undertaking. In this context, it is not sufficient that there are agreements between two or more parties having an equal shareholding in the capital of an undertaking which establish identical rights and powers between the parties. For example, in the case of an undertaking where three shareholders each own one-third of the share capital and each elect one-third of the members of the Board of Directors, the shareholders do not have joint control since decisions are required to be taken on the basis of a simple majority. The same considerations also apply in more complex structures, for example, where the capital of an undertaking is equally divided between three shareholders and where the Board of Directors is composed of twelve members, each of the shareholders A, B and C electing two, another two being elected by A, B and C jointly, whilst the remaining four are chosen by the other eight members jointly. In this case also there is no joint control, and hence no control at all within the meaning of the Merger Regulation.

2.4. *Other considerations related to joint control*

36. Joint control is not incompatible with the fact that one of the parent companies enjoys specific knowledge of and experience in the business of the joint venture. In such a case, the other parent company can play a modest or even non-existent role in the daily management of the joint venture where its presence is motivated by considerations of a financial, long-term-strategy, brand image or general policy nature. Nevertheless, it must always retain the real possibility of contesting the decisions taken by the other parent company, without which there would be sole control.

37. For joint control to exist, there should not be a casting vote for one parent company only. However, there can be joint control when this casting vote can be exercised only after a series of stages of arbitration and attempts at reconciliation or in a very limited field ([24]).

2.5. *Joint control for a limited period*

38. Where an operation leads to joint control for a starting-up period ([25]) but, according to legally binding agreements, this joint control will be converted to sole control by one of the shareholders, the whole operation will normally be considered to be an acquisition of sole control.

3. **Control by a single shareholder on the basis of veto rights**

39. An exceptional situation exists where only one shareholder is able to veto strategic decisions in an undertaking, but this shareholder does not have the power, on his own, to impose such decisions. This situation occurs either where one shareholder holds 50 % in an undertaking whilst the remaining 50 % is held by two or more minority shareholders, or where there is a quorum required for strategic decisions which in fact confers a veto right upon only one minority shareholder ([26]). In these circumstances, a single shareholder possesses the same level of influence as that normally enjoyed by several jointly-controlling shareholders, i. e. the power to block the adoption of strategic

([24]) Case IV/M.425 — British Telecom/Banco Santander, of 28 March 1994.

([25]) This starting-up period must not exceed three years. Case IV/M.425 — British Telecom/Banco Santander, *ibid*.

([26]) Case IV/M.258 — CCIE/GTE, of 25 September 1992, where the veto rights of only one shareholder were exercisable through a member of the board appointed by this shareholder.

decisions. However, this shareholder does not enjoy the powers which are normally conferred on an undertaking with sole control, i. e. the power to impose strategic decisions. Since this shareholder can produce a deadlock situation comparable to that in normal cases of joint control, he acquires decisive influence and therefore control within the meaning of the Merger Regulation ([27]).

4. Changes in the structure of control

40. A concentration may also occur where an operation leads to a change in the structure of control. This includes the change from joint control to sole control as well as an increase in the number of shareholders exercising joint control. The principles for determining the existence of a concentration in these circumstances are set out in detail in the Notice on the concept of undertakings concerned ([28]).

IV. EXCEPTIONS

41. Article 3(5) sets out three exceptional situations where the acquisition of a controlling interest does not constitute a concentration under the Merger Regulation.

42. First, the acquisition of securities by companies whose normal activities include transactions and dealing in securities for their own account or for the account of others is not deemed to constitute a concentration if such an acquisition is made in the framework of these businesses and if the securities are held on only a temporary basis (Article 3(5)(a)). In order to fall within this exception, the following requirements must be fulfilled:

— the acquiring undertaking must be a credit or other financial institution or insurance company the normal activities of which are described above,

— the securities must be acquired with a view to their resale,

— the acquiring undertaking must not exercise the voting rights with a view to determining the strategic commercial behaviour of the target company or must exercise these rights only with a view to preparing the total or partial disposal of the undertaking, its assets or securities,

— the acquiring undertaking must dispose of its controlling interest within one year of the date of the acquisition, that is, it must reduce its shareholding within this one-year period at least to a level which no longer confers control. This period, however, may be extended by the Commission where the acquiring undertaking can show that the disposal was not reasonably possible within the one-year period.

43. Secondly, there is no change of control, and hence no concentration within the meaning of the Merger Regulation, where control is acquired by an office-holder according to the law of a Member State relating to liquidation, winding-up, insolvency, cessation of payments, compositions or analogous proceedings (Article 3(5)(b));

44. Thirdly, a concentration does not arise where a financial holding company within the meaning of the Fourth Council Directive 78/660/EEC ([29]) acquires control, provided that this company exercises its voting rights only to maintain the full value of its investment and does not otherwise determine directly or indirectly the strategic commercial conduct of the controlled undertaking.

45. In the context of the exceptions under Article 3(5), the question may arise whether a rescue operation constitutes a concentration under the Merger Regulation. A rescue operation typically involves the conversion of existing debt into a new company, through which a syndicate of banks may acquire joint control of the company concerned.

([27]) Since this shareholder is the only undertaking acquiring a controlling influence, only this shareholder is obliged to submit a notification under the Merger Regulation.

([28]) Paragraphs 30 to 48.

([29]) OJ L 222, 14.8.1978, p. 11, as last amended by the Act of Accession of Austria, Finland and Sweden. Article 5(3) of this Directive defines financial holding companies as 'those companies the sole objective of which is to acquire holdings in other undertakings, and to manage such holdings and turn them to profit, without involving themselves directly or indirectly in the management of those undertakings, the foregoing without prejudice to their rights as shareholders'.

Where such an operation meets the criteria for joint control, as outlined above, it will normally be considered to be a concentration ([30]). Although the primary intention of the banks is to restructure the financing of the undertaking concerned for its subsequent resale, the exception set out in Article 3(5)(a) is normally not applicable to such an operation. This is because the restructuring programme normally requires the controlling banks to determine the strategic commercial behaviour of the rescued undertaking. Furthermore, it is not normally a realistic proposition to transform a rescued company into a commercially viable entity and to resell it within the permitted one-year period. Moreover, the length of time needed to achieve this aim may be so uncertain that it would be difficult to grant an extension of the disposal period.

V. FINAL

46. The Commission's interpretation of Article 3 as set out in this Notice is without prejudice to the interpretation which may be given by the Court of Justice or the Court of First Instance of the European Communities.

([30]) Case IV/M.116 — Kelt/American Express, of 28 August 1991.